

**United Nations  
Commission on  
International  
Trade Law**

**YEARBOOK**

**Volume XII: 1981**



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# NOTE

Symbols of United Nations documents are composed of capital letters combined with figures. Mention of such a symbol indicates a reference to a United Nations document.

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## INTRODUCTION

This is the twelfth volume in the series of Yearbooks of the United Nations Commission on International Trade Law (UNCITRAL).<sup>1</sup>

The present volume consists of three parts. Part One contains the Commission's report on the work of its fourteenth session, which was held in Vienna from 19 to 26 June 1981, and the action thereon by the United Nations Conference on Trade and Development (UNCTAD) and by the General Assembly.

Part Two reproduces most of the documents considered at the fourteenth session of the Commission. These documents include reports of the Commission's three Working Groups dealing respectively with international contract practices, international negotiable instruments and the new international economic order, as well as reports and notes by the Secretary-General and the Secretariat. Also included in this part are selected working papers which were before the Working Groups.

Part Three contains relevant resolutions of the General Assembly, a bibliography of recent writings related to the Commission's work, prepared by the Secretariat, and a check list of UNCITRAL documents.

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<sup>1</sup> To date the following volumes of the *Yearbook of the United Nations Commission on International Trade Law* [abbreviated herein as *Yearbook* . . . (year)] have been published:

<i>Volume</i>	<i>Years covered</i>	<i>United Nations Publication, Sales No.</i>
I	1968-1970	E.71.V.1
II	1971	E.72.V.4
III	1972	E.73.V.6
IV	1973	E.74.V.3
V	1974	E.75.V.2
VI	1975	E.76.V.5
VII	1976	E.77.V.1
VIII	1977	E.78.V.7
IX	1978	E.80.V.8
X	1979	E.81.V.2
XI	1980	E.81.V.8

## THE FOURTEENTH SESSION (1981)

### A. Report of the United Nations Commission on International Trade Law on the work of its fourteenth session (Vienna, 19-26 June 1981) (A/36/17)\*

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#### INTRODUCTION

1. The present report of the United Nations Commission on International Trade Law covers the Commission's fourteenth session, held at Vienna from 19 to 26 June 1981.

2. Pursuant to General Assembly resolution 2205 (XXI) of 17 December 1966, this report is submitted to the General Assembly and is also submitted for comments to the United Nations Conference on Trade and Development.

\* Official Records of the General Assembly, Thirty-sixth Session, Supplement No. 17 (hereinafter referred to as "Report").

#### CHAPTER I. ORGANIZATION OF THE SESSION

##### A. Opening

3. The United Nations Commission on International Trade Law (UNCITRAL) commenced its fourteenth session on 19 June 1981. The session was opened on behalf of the Secretary-General by Mr. Erik Suy, the Legal Counsel.

##### B. Membership and attendance

4. General Assembly resolution 2205 (XXI) established the Commission with a membership of 29 States, elected by the Assembly. By resolution 3108 (XXVIII), the General Assembly increased the membership of the Commission from 29 to 36 States. The present members

of the Commission, elected on 15 December 1976 and 9 November 1979, are the following States:<sup>1</sup> Australia,\* Austria,\* Burundi,\* Chile,\* Colombia,\* Cuba,\*\* Cyprus,\*\* Czechoslovakia,\*\* Egypt,\* Finland,\* France,\* German Democratic Republic,\* Germany, Federal Republic of,\*\* Ghana,\* Guatemala,\*\* Hungary,\*\* India,\*\* Indonesia,\* Iraq,\*\* Italy,\*\* Japan,\* Kenya,\*\* Nigeria,\* Peru,\*\* Philippines,\*\* Senegal,\*\* Sierra Leone,\*\* Singapore,\* Spain,\*\* Trinidad and Tobago,\*\* Uganda,\*\* Union of Soviet Socialist Republics,\* United Kingdom of Great Britain and Northern Ireland,\* United Republic of Tanzania,\* United States of America\*\* and Yugoslavia.\*\*

5. With the exception of Burundi, Colombia, Cyprus, Peru, Senegal and the United Republic of Tanzania, all members of the Commission were represented at the session.

6. The session was also attended by observers from the following States: Argentina, Bolivia,\*\*\* Brazil, Bulgaria, Canada, China, Costa Rica, Ecuador,\*\*\* Gabon, Greece, Holy See, Lebanon, Luxembourg, Malaysia, Mexico, Netherlands, Norway, Pakistan, Panama, Poland, Portugal, Republic of Korea, Romania, Suriname, Switzerland, Thailand,\*\*\* Tunisia, Turkey, Uruguay and Venezuela.

\* Term of office expires on the day before the opening of the regular annual session of the Commission in 1983.

\*\* Term of office expires on the day before the opening of the regular annual session of the Commission in 1986.

\*\*\* Correction to original report.

Pursuant to General Assembly resolution 2205 (XXI), the members of the Commission are elected for a term of six years, except that, in connexion with the initial election, the terms of 14 members, selected by the President of the Assembly by drawing lots, expired at the end of three years (31 December 1970); the terms of the 15 other members expired at the end of six years (31 December 1973). Accordingly, the General Assembly, at its twenty-fifth session, elected 14 members to serve for a full term of six years, ending on 31 December 1976, and, at its twenty-eighth session, elected 15 members to serve for a full term of six years, ending on 31 December 1979. The General Assembly, at its twenty-eighth session, also selected seven additional members. Of these additional members, the term of three members, selected by the President of the Assembly by drawing lots, would expire at the end of three years (31 December 1976) and the term of four members would expire at the end of six years (31 December 1979). To fill the vacancies on the Commission which would occur on 31 December 1976, the General Assembly, at its thirty-first session, on 15 December 1976, elected (or re-elected) 17 members to the Commission. Pursuant to resolution 31/99 of 15 December 1976, the new members took office on the first day of the regular annual session of the Commission immediately following their election (23 May 1977) and their term will expire on the last day prior to the opening of the seventh regular annual session of the Commission following their election (in 1983). In addition, the term of office of those members whose term would expire on 31 December 1979 was by the same resolution extended till the last day prior to the beginning of the regular annual session of the Commission in 1980. To fill the vacancies that would occur on that date, the General Assembly, at its thirty-fourth session, on 9 November 1979, elected (or re-elected) 19 members to the Commission. Pursuant to resolution 31/99 of 15 December 1976, the new members took office on the first day of the regular annual session of the Commission immediately following their election (14 July 1980) and their term will expire on the last day prior to the opening of the seventh regular annual session of the Commission following their election (in 1986).

7. The following United Nations organs, specialized agency, intergovernmental organizations and international non-governmental organization were represented by observers:

(a) *United Nations organs*

Economic Commission for Europe and the United Nations  
Industrial Development Organization.

(b) *Specialized agency*

International Monetary Fund.

(c) *Intergovernmental organizations*

Bank for International Settlements, Council for Mutual Economic Assistance, Council of Europe, European Communities, Hague Conference on Private International Law, International Institute for the Unification of Private Law and Organization of American States.

(d) *International non-governmental organization*

International Chamber of Commerce.

### C. Election of officers

8. The Commission elected the following officers by acclamation:<sup>2</sup>

Chairman ..... Mr. L. H. Khoo (Singapore)

**Vice-Chairmen ..... Mr. R. Eyzaguirre (Chile)**

Mr. E. Sam (Ghana)

Mr. I. Szász (Hungary)

Rapporteur ..... Mr. A. Dúček (Austria)

#### D. Agenda

9. The agenda of the session, as adopted by the Commission at its 243rd meeting on 19 June 1981, was as follows:

1. Opening of the session.
2. Election of officers.
3. Adoption of the agenda: tentative schedule of meetings.
4. International contract practices.
5. International payments.
6. International commercial arbitration.
7. New international economic order: industrial contracts.
8. Co-ordination of work.

<sup>2</sup> The elections took place at the 245th meeting on 22 June 1981 and the 247th meeting on 23 June 1981. In accordance with a decision taken by the Commission at its first session, the Commission has three Vice-Chairmen, so that, together with the Chairman and Rapporteur, each of the five groups of States listed in General Assembly resolution 2205 (XXI), sect. 11, para. 1, will be represented on the bureau of the Commission (see *Official Records of the General Assembly, Twenty-third Session, Supplement No. 16 (A/7216)*, para. 14 (Yearbook . . . 1968-1970, part two, I, A)). As the election of the Chairman was postponed until 22 June 1981, the Secretary of the Commission functioned as the Chairman during the 243rd and 244th meetings on 19 June 1981. The Legal Counsel pointed out that this procedure should not set a precedent, and could only be regarded as a provisional measure adopted in order to expedite the work of the Commission.

9. Status of conventions.
10. Training and assistance in the field of international trade law.
11. Future work.
12. Other business.
13. Adoption of the report of the Commission.

#### E. Decisions of the Commission

10. The decisions taken by the Commission in the course of its fourteenth session were all reached by consensus.

#### F. Adoption of the report

11. The Commission adopted the present report at its 251st meeting, on 26 June 1981.

### CHAPTER II. INTERNATIONAL PAYMENTS

#### A. Draft Convention on International Bills of Exchange and International Promissory Notes, and Uniform Rules on International Cheques<sup>3</sup>

##### Introduction

12. The Commission had before it the report of the Working Group on International Negotiable Instruments on the work of its tenth session held at Vienna from 5 to 16 January 1981 (A/CN.9/196).<sup>\*</sup> The report set forth the progress made by the Working Group at this session on the preparation of a draft Convention on International Bills of Exchange and International Promissory Notes, and on the preparation of Uniform Rules on International Cheques. The proposed instruments would establish uniform rules applicable to an international instrument (bill of exchange, promissory note or cheque) for optional use in international payments. The Commission also had before it a note by the Secretariat entitled "Alternative methods for the final adoption of conventions emanating from the work of the Commission" (A/CN.9/204)<sup>\*\*</sup> which, *inter alia*, examined alternative methods for the final adoption of the draft Convention and the Uniform Rules.

13. The report of the Working Group noted that the Working Group continued its preliminary exchange of views on the Uniform Rules on International Cheques, and considered articles 34 to 86 and draft articles A to F relating to crossed cheques as drafted by the Secretariat (A/CN.9/WG.IV/WP.15 and A/CN.9/WG.IV/WP.19).

The Working Group also examined legal issues arising outside the cheque submitted to the Working Group by the Secretariat (A/CN.9/196, paras. 191-199), issues relating to post-dated cheques (A/CN.9/196, paras. 200-203), and certain other issues (A/CN.9/196, paras. 204-207).

14. As regards its future work, the Working Group considered whether the draft Convention on International Bills of Exchange and International Promissory Notes and the Uniform Rules on International Cheques were to be drafted as separate texts, or consolidated in a single text. The Working Group expressed the opinion that, although there was considerable similarity between the law governing bills of exchange and promissory notes on the one hand, and cheques on the other, there were inherent in the use of cheques special features which distinguished these instruments from bills of exchange and promissory notes. One important feature was that the bill of exchange and promissory note were primarily credit instruments, while the essential feature of a cheque was that it was a payment instrument. Moreover, in civil law countries the bill of exchange and promissory note on the one hand, and the cheque on the other, were traditionally seen as different instruments and were traditionally governed by separate legal texts. The Working Group therefore suggested that the Commission should agree on the adoption of two separate draft texts (A/CN.9/196, paras. 208-210).

15. The Working Group was of the view that it would probably be able to complete its work at its eleventh session, scheduled to be held in New York from 3 to 14 August 1981. The Working Group also noted that it would accord with past practice for the Secretary-General to transmit the draft texts adopted by the Working Group, upon their completion, together with a commentary, to Governments and interested international organizations for comments. In this connexion the Working Group suggested to the Commission that it might wish to consider, in the light of the comments received, whether, for purposes of accelerating the work, it should request the Working Group to study and consider those comments and report to the Commission (A/CN.9/196, paras. 211-213).

##### Discussion at the session

16. As regards the future work, there was general agreement that the draft Convention and the Uniform Rules should be drafted by the Working Group as two separate texts. There was also general agreement that the work should be completed by the Working Group as expeditiously as possible, and that if the work could not be completed at the eleventh session of the Working Group, a further session should be held. It was also agreed that, upon completion of the draft texts by the Working Group, they should be circulated, with a commentary, to all Governments and interested international organiza-

<sup>\*</sup> Reproduced in this volume, part two, II, A.

<sup>\*\*</sup> Reproduced in this volume, part two, VIII.

<sup>3</sup> The Commission considered this subject at its 243rd and 244th meetings, on 19 June 1981.

tions for comments. It was noted that sufficient time should be given to Governments and interested organizations for the purpose of examining these complex texts and formulating their comments. The view was also expressed that, in order to assist Governments to make their comments, the commentary which would accompany the texts should indicate, to the extent possible, the relationship of the provisions of the draft Convention and the Uniform Rules to the provisions of the Convention providing a Uniform Law for Bills of Exchange and Promissory Notes, Geneva, 1930, and the Convention providing a Uniform Law for Cheques, Geneva, 1931.

17. Different views were expressed as to the proper procedure to be followed after the comments were received. Under one view, the comments should be referred for consideration to the Working Group, which should revise the texts, if appropriate, in the light of the comments. Thereafter the revised texts, with a report by the Working Group on the action taken by it, should be submitted to the Commission, and the Commission could thereafter devote some time during a session to examine and approve the texts. In this context, a view was expressed that if the comments were made available to members of the Commission that were not members of the Working Group, before the Working Group commenced the review, it would assist those non-members of the Working Group in assessing the need to send observers to the Working Group session.

18. Under another view, the comments should be referred to the Commission, which should examine the texts in detail in the light of the comments, and revise them as appropriate.

19. In support of the former view it was noted that a revision of the draft texts in the light of the comments received could more expeditiously be undertaken by the Working Group than by the Commission. Furthermore, the prior revision of the texts by the Working Group would considerably expedite the work when the Commission came to consider the texts. It was suggested that a detailed examination of the two texts without such a prior review might result in the Commission having to devote an inordinate length of time to this work because of the highly complex and technical nature of the subjects. Accordingly, thought should be given at least to the advisability of adopting appropriate procedures which would, whilst not affecting the quality of the work, reduce the period of time needed for the conclusion of such a convention or conventions. It was noted that all States were free to attend sessions of the Working Group as observers, and that several States did so attend, and as a result the approval of the texts by the Working Group was one whose scope extended beyond the membership of the Working Group. Another suggestion in this context was for an enlargement of the membership of the

Working Group for the purposes of revising the texts after the comments had been received.

20. In support of the latter view, it was noted that texts submitted by the Commission to the General Assembly, and later to a Diplomatic Conference, should carry the full approval of the Commission. Such approval could only be secured by a careful examination of the texts by the Commission itself. Furthermore, time would not be saved by a prior revision of the texts by the Working Group in the light of the comments received, as it would be difficult to prevent questions settled by the Working Group from being re-opened during the deliberations of the Commission. It was also observed that, although States not members of the Working Group could attend sessions of the Working Group as observers, many States, particularly the developing States, were unable due to budgetary constraints to send representatives as observers. Moreover, the apprehension that a careful examination of the texts by the Commission might take an inordinate length of time was unjustified.

21. After deliberation, the Commission agreed to defer its decision on the exact procedure to be followed after comments had been received and decided that it should revert to this question at its fifteenth session after the work had been completed by the Working Group. It was agreed, however, that after the texts had been finalized by the Commission, the appropriate procedure for their adoption as a convention or conventions would be through a Diplomatic Conference, and not through their adoption by the General Assembly upon a recommendation by the Sixth Committee.

#### *Decision of the Commission*

22. At its 244th meeting, on 19 June 1981, the Commission adopted the following decision:

#### *The United Nations Commission on International Trade Law*

1. *Takes note with appreciation* of the report of the Working Group on International Negotiable Instruments on the work of its tenth session;

2. *Requests* the Working Group to continue its work under its present terms of reference and to complete that work expeditiously;

3. *Endorses* the decision of the Working Group to hold its eleventh session in August 1981 and authorizes it to hold a further session if the work so requires;

4. *Decides* that the Working Group should draw up the draft Convention on International Bills of Exchange and International Promissory Notes, and the Uniform Rules on International Cheques, as separate texts and not as a consolidated text;

5. *Requests* the Secretary-General, after the completion of the texts by the Working Group, to circulate

them, together with a commentary, to all governments and interested international organizations for their comments.

### B. *Universal unit of account for international conventions*<sup>4</sup>

#### *Introduction*

23. At its eleventh session the Commission decided that it "should study ways of establishing a system for determining a universal unit of account of constant value which would serve as a point of reference in international conventions for expressing amounts in monetary terms".<sup>5</sup>

24. The proposal was examined by the UNCITRAL Study Group on International Payments at its meetings in 1978, 1979 and 1980. The Study Group was of the view that the most desirable approach was to combine the use of the Special Drawing Right (SDR) with a suitable index which would preserve over time the purchasing power of the monetary values set forth in the international conventions in question.

25. At its present session the Commission had before it a report of the Secretary-General entitled "Universal unit of account for international conventions" (A/CN.9/200)\* reflecting the view of the Study Group and containing an annex prepared by the Staff of the International Monetary Fund at the request of the Commission's Secretariat. That annex explained many of the considerations which had led to the Study Group's recommendation.

26. The report suggested that if the Commission agreed that it would be desirable to prepare such a provision for use in international conventions, it might wish to adopt the provision at its next session since several conventions for which such a provision might be appropriate were in the process of elaboration by other organizations.

#### *Discussion at the session*

27. There was general agreement that the erosion of the purchasing value of the maximum compensation recoverable under conventions which specify a limit of liability was a serious problem. It was recognized that as a result the limit of liability must be adjusted periodically.

28. Under one view no automatic adjustment formula should be adopted. It was stated that indexing con-

tributed to inflation. Moreover, the erosion of currencies was not the only reason for changing the limit of liability. Technical changes, such as a change in the nature of the cargo carried, might also justify a change in the limit of liability. These factors could only be taken into account by a revision conference.

29. The view was also expressed that any provision which the Commission might adopt could be expected to be used only in connexion with new conventions and not in connexion with existing ones.

30. Under another view recent experience had shown such rapid generalized inflation that a revision conference would need to be held at least every five years for each convention in question if the limits of liability were not to deteriorate excessively. Only an automatic adjustment formula could be expected to work reasonably well in this situation.

31. There was no agreement on the nature of the automatic adjustment mechanism which might be used. Some concern was expressed for the problems of non-member States of the International Monetary Fund if an index were to be based on the SDR. It was pointed out that some provision similar to article 26 of the Hamburg Rules and based upon the gold value would be necessary in this respect. Moreover, in regard to the idea of using an index, some representatives reserved their position since the report had been received by them only in the course of the present session, and therefore could not be properly studied.

32. After discussion the Commission agreed to refer the matter to the Working Group on International Negotiable Instruments. The Working Group was requested to consider various possibilities in regard to the formulation of a unit of account of constant value and to prepare a text, if possible. The Secretary-General was requested to conduct such studies as seemed desirable in the light of the discussion in the present session of the Commission and to submit those studies to the Working Group.

### C. *Electronic funds transfer*<sup>6</sup>

#### *Introduction*

33. The Commission, at its eleventh session, included as an item in its programme of work the legal problems arising out of electronic funds transfer.<sup>7</sup> The work was entrusted to the UNCITRAL Study Group on International Payments. At its thirteenth session the Commission requested the Secretariat to submit to it at its fourteenth session a progress report on the matter, so that it

\* Reproduced in this volume, part two, II, C.

<sup>4</sup> The Commission considered this subject at its 246th meeting, on 22 June 1981.

<sup>5</sup> A/CN.9/156; Report of the United Nations Commission on International Trade Law on the work of its eleventh session, *Official Records of the General Assembly, Thirty-third Session, Supplement No. 17 (A/33/17)*, para. 67 (c) (iii) (Yearbook . . . 1978, part one, II, A).

<sup>6</sup> The Commission considered this subject at its 246th meeting, on 22 June 1981.

<sup>7</sup> Report of the United Nations Commission on International Trade Law on the work of its eleventh session, *Official Records of the General Assembly, Thirty-third Session, Supplement No. 17 (A/33/17)*, para. 67 (c) (ii) (Yearbook . . . 1978, part two, II, A).

might give directions on the scope of further work after having considered the Study Group's conclusions.<sup>8</sup>

34. The Commission at its present session had before it a note by the Secretary-General entitled "Electronic funds transfer" (A/CN.9/199)\* which stated that, since the Study Group had not met between the thirteenth and fourteenth sessions of the Commission, the Secretariat was unable to submit to the Commission any information in addition to that previously submitted which would aid the Commission in giving directives on the scope of further work.

35. The report also stated that the Secretariat would request the Study Group at its next meeting in August 1981 to recommend to the Commission whether the Commission should undertake substantive work in this field at the present time, and, if so, what the nature of that work might be.

#### *Action by the Commission*

36. The Commission took note of the report.

### CHAPTER III. INTERNATIONAL TRADE CONTRACTS

#### *A. Uniform rules on liquidated damages and penalty clauses<sup>9</sup>*

##### *Introduction*

37. At its twelfth session, the Commission decided that work should be undertaken directed to the formulation of uniform rules regulating liquidated damages and penalty clauses and entrusted the work to its Working Group on International Contract Practices, with a mandate to consider the feasibility of formulating uniform rules on liquidated damages and penalty clauses applicable to a wide range of international trade contracts.<sup>10</sup>

38. At the present session, the Commission had before it the report of the Working Group on the work of its second session, held in New York from 13 to 17 April 1981 (A/CN.9/197).\*\* The report of the Working Group indicated that it had prepared a set of draft uniform rules on liquidated damages and penalty clauses (A/CN.9/197, annex), and had completed its mandate. The Working

Group had, however, decided that the issue of the form that the rules might take should be left for decision by the Commission. It had also noted that, depending on the form that the rules might take, certain supplementary provisions might be needed, and that the Secretariat might be requested to draft such provisions (A/CN.9/197, paras. 46-48).

39. The Commission also had before it a report of the Secretary-General entitled "Question of co-ordination: direction of the work of the Commission" (A/CN.9/203),\* and a note by the Secretariat entitled "Alternative methods for the final adoption of conventions emanating from the work of the Commission" (A/CN.9/204).\*\* The former report, in considering the final form of texts which might be adopted by the Commission, *inter alia*, examined as an example the draft uniform rules adopted by the Working Group, and set forth the advantages and disadvantages of casting the rules in the form of a convention, a model law, or a recommendation (A/CN.9/203, paras. 114-122). The latter note considered the possible future procedure to be followed in respect of the draft uniform rules, and noted, *inter alia*, that if the form of a convention were decided upon, it might be possible for such convention to be adopted by the General Assembly on the recommendation of the Sixth Committee rather than by a diplomatic conference.

##### *Discussion at the session*

40. The discussion focused on the possible form of the draft uniform rules. Some support was expressed for the form of a convention, as it was the most effective type of unifying instrument. On the other hand, it was observed that the limited scope of the rules made a convention inappropriate. In this connexion the view was expressed that it would be of interest for the Commission to know whether the Sixth Committee would be prepared to devote a part of one of its annual sessions to an examination of the draft uniform rules, as that knowledge might be relevant to a determination of the form of the rules by the Commission.

41. Some support was also expressed for the form of recommendation. It was noted that the substantive work involved could be completed within the Commission itself. Furthermore, a recommendation could have a wide scope, being addressed both to States to make their law conform to the uniform rules, and to the business community to apply by agreement the uniform rules to the extent possible to their international contracts. On the other hand, it was pointed out that an agreement of the contracting parties in regard to the applicability of the rules might be ineffective, since they concerned matters which in many national laws were governed by mandatory provisions which differed from country to country.

\* Reproduced in this volume, part two, II, B.

\*\* Reproduced in this volume, part two, I, A.

<sup>8</sup> Report of the United Nations Commission on International Trade Law on the work of its thirteenth session, *Official Records of the General Assembly, Thirty-fifth Session, Supplement No. 17* (A/35/17), para. 163 (Yearbook . . . 1980, part one, II, A).

<sup>9</sup> The Commission considered this subject at its 244th meeting, on 19 June 1981.

<sup>10</sup> Report of the United Nations Commission on International Trade Law on the work of its twelfth session, *Official Records of the General Assembly, Thirty-fourth Session, Supplement No. 17* (A/34/17), para. 31 (Yearbook . . . 1979, part one, II, A).

\* Reproduced in this volume, part two, V, B.

\*\* Reproduced in this volume, part two, VIII.

42. The greatest support was expressed for the form of a model law. A model law had the advantage that it could later form the basis of a convention. As in the case of a recommendation, the substantive work involved could be completed within the Commission itself.

43. After deliberation, there was general agreement that a decision on the issue of form should be deferred to a later session. The procedure for the immediate future should be that the draft uniform rules, incorporating supplementary provisions to be drafted by the Secretariat, should be circulated to all Governments and interested international organizations, together with a commentary to be prepared by the Secretariat. In drafting the supplementary provisions, the Secretariat should take into account the relevant provisions of the Conventions which have emerged from the work of the Commission. The draft uniform rules, when circulated, should also be accompanied by a questionnaire seeking to elicit the views of Governments and international organizations on the most appropriate form for the rules.

#### *Decision by the Commission*

44. At its 244th meeting, on 19 June 1981, the Commission adopted the following decision:

#### *The United Nations Commission on International Trade Law*

1. *Takes note with appreciation* of the report of the Working Group on International Contract Practices on the work of its second session;

2. *Congratulates* the Working Group on the expeditious completion of the mandate entrusted to it;

3. *Requests* the Secretary-General:

(a) To incorporate in the draft uniform rules on liquidated damages and penalty clauses prepared by the Working Group such supplementary provisions as might be required if the rules were to take the form of a convention or a model law;

(b) To prepare a commentary on the draft uniform rules;

(c) To prepare a questionnaire addressed to Governments and international organizations seeking to elicit their views on the most appropriate form for the uniform rules; and

(d) To circulate the draft uniform rules to all Governments and interested international organizations for their comments, together with the commentary and the questionnaire;

4. *Decides* that, if the procedures set forth above are completed in time, the consideration of the draft uniform rules should be placed on the agenda of the fifteenth session.

#### *B. Clauses protecting parties against the effects of currency fluctuations<sup>11</sup>*

##### *Introduction*

45. The Commission, at its twelfth session, had before it a report of the Secretary-General entitled "Clauses protecting parties against the effects of currency fluctuations" which described the commercial reasons for clauses designed to protect creditors against changes of the value of a currency in relation to other currencies and for clauses by which creditors seek to maintain the purchasing value of the monetary obligation under the contract (A/CN.9/164).<sup>\*</sup> The report examined the various kinds of clauses designed to accomplish these two results and considered the legal and policy framework in which such clauses operate in a selected number of countries.

46. The Commission, at its twelfth session, recognized that the subject was of current interest because of the floating of the major trade currencies.<sup>12</sup> However, doubts were expressed whether it was possible for the Commission to regulate on a world-wide basis the content of clauses to eliminate most or all of the monetary risks involved in long-term contracts.

47. As a result, the Commission requested the Secretariat to carry out further studies in respect of clauses protecting parties against the effects of currency fluctuations.

48. At the present session the Commission had before it a report of the Secretary-General entitled "Clauses protecting parties against the effects of currency fluctuations" (A/CN.9/201)<sup>\*\*</sup> which noted that the Secretariat was currently studying the problems caused by currency fluctuations in two contexts:

The creation of a universal unit of account of constant value for use in international conventions. Such a unit of account would be of relevance to some international contracts.

Studies in respect of the price term in contracts for the supply and construction of large industrial works, including the clause on price revision and the clause on currency and rates of exchange. These studies are to be presented to the third session of the Working Group on the New International Economic Order.

##### *Discussion at the session*

49. It was pointed out that the fluctuation in value of the major trade currencies was a great problem for the

<sup>\*</sup> Yearbook . . . 1979, part two, I, D.

<sup>\*\*</sup> Reproduced in this volume, part two, I, C.

<sup>11</sup> The Commission considered this subject at its 245th meeting, on 22 June 1981.

<sup>12</sup> Report of the United Nations Commission on International Trade Law on the work of its twelfth session, *Official Records of the General Assembly, Thirty-fourth Session, Supplement No. 17 (A/34/17)*, paras. 32-40 (Yearbook . . . 1979, part one, II, A).



developing countries as well as for the countries whose currencies were in use. Therefore, there was general agreement that the Secretariat should continue to study the question of currency fluctuation clauses and report at a future session of the Commission. It was also suggested that the Secretariat might expand the scope of its inquiry beyond the areas currently under study.

#### CHAPTER IV. INTERNATIONAL COMMERCIAL ARBITRATION

##### A. UNCITRAL Arbitration Rules: administrative guidelines<sup>13</sup>

###### Introduction

50. The Commission, at its twelfth session, considered certain issues relevant in the context of the UNCITRAL Arbitration Rules.<sup>14</sup> One issue was whether the Commission should take steps to facilitate the use of the Rules in administered arbitration and seek to prevent disparity in their use by arbitral institutions. The Commission, at that session, decided to request the Secretary-General:

"To prepare for the next session, if possible in consultation with interested international organizations, guidelines for administering arbitration under the UNCITRAL Arbitration Rules, or a check-list of issues which may arise when the UNCITRAL Arbitration Rules are used in administered arbitration."<sup>15</sup>

51. Pursuant to this request, the Secretariat prepared, and submitted to the Commission at its thirteenth session, a note entitled "International commercial arbitration—issues relating to the use of the UNCITRAL Arbitration Rules and the designation of an appointing authority" (A/CN.9/189)\* which took into account the views expressed by the Commission and information obtained in consultative meetings with members of the International Council for Commercial Arbitration and representatives of the International Chamber of Commerce. The note suggested, and set forth, guidelines which could assist arbitral institutions in formulating rules for administering arbitrations under the UNCITRAL Arbitration Rules and which would encourage them to leave these Rules unchanged.

52. The Commission, at its thirteenth session, held a brief exchange of views during which support was expressed for the idea of preparing guidelines in the form

of recommendations and for the approach taken in the draft guidelines.<sup>16</sup> However, the Commission decided, in order to give representatives sufficient time to consult with interested circles, not to discuss the contents of the draft guidelines in detail and to postpone their consideration to the next session.<sup>17</sup>

###### Discussion at the session

53. The Commission discussed the desirability of issuing guidelines for administering arbitrations under the UNCITRAL Arbitration Rules and considered the draft recommendations set forth in the note by the Secretariat (A/CN.9/189).\*

54. The Commission, after deliberation, was agreed that the issuance of guidelines in the form of recommendations could serve a useful purpose in assisting institutions willing to act as appointing authority or in providing administrative services in cases conducted under the UNCITRAL Arbitration Rules. In support of this, it was stated that such guidelines might help to avoid disparity in the application of these Rules by different institutions and to enhance the parties' certainty as to what procedures to expect. Furthermore, it was agreed that such guidelines should be addressed not only to arbitral institutions but also to other bodies, e.g. chambers of commerce, which, too, might be willing to act as appointing authority or provide administrative services as envisaged under the guidelines.

55. As to the draft text of the guidelines prepared by the Secretariat (A/CN.9/189, paragraph 15),\* various amendments were submitted. Some of these amendments, and the discussion thereon, revealed a certain difference of opinion as to any effort to discourage institutions from adopting administrative procedures which would modify the UNCITRAL Arbitration Rules. Under one view, the guidelines should attempt to ensure, for the sake of uniform application and certainty of parties, that these Rules be left unchanged, to the extent possible. Under another view, the guidelines should not prevent institutions from adopting procedures which modify these Rules according to their specific institutional needs.

56. These latter concerns were primarily aimed at the situation where an institution uses the UNCITRAL Arbitration Rules as a model in adopting its own institutional rules and not so much at the situation where the institution merely adopts procedures for providing administrative services in cases to be conducted under the UNCITRAL Arbitration Rules. It was suggested in this connexion, that these two situations be more clearly distinguished and that the guidelines should deal primarily,

\* Yearbook . . . 1980, part two, IV, D.

<sup>13</sup> The Commission considered this subject at its 248th meeting, on 23 June 1981.

<sup>14</sup> Report of the United Nations Commission on International Trade Law on the work of its twelfth session, *Official Records of the General Assembly, Thirty-fourth Session, Supplement No. 17 (A/34/17)*, paras. 57-66 (Yearbook . . . 1979, part one, II, A).

<sup>15</sup> *Ibid.*, para. 71, subpara. 2 (a).

\* Yearbook . . . 1980, part two, IV, D.

<sup>16</sup> Report of the United Nations Commission on International Trade Law on the work of its thirteenth session, *Official Records of the General Assembly, Thirty-fifth Session, Supplement No. 17 (A/35/17)*, paras. 110-111 (Yearbook . . . 1980, part one, II, A).

<sup>17</sup> *Ibid.*, para. 113, subpara. 3.

if not exclusively, with the latter situation. It was agreed that the guidelines, whatever their final stand on this issue of modifications, should contain a recommendation to identify clearly any such modification by way of a reference to the modified provision of the UNCITRAL Arbitration Rules.

57. Other proposals submitted were specific amendments to the draft text of the guidelines aimed at clarifying matters and fully aligning the recommendations with the pertinent provisions of the UNCITRAL Arbitration Rules. It was also suggested that the guidelines state expressly that the services envisaged and the points mentioned therein were not intended to be exhaustive.

58. The Commission, after deliberation, was agreed that further consideration was needed of the amendments proposed and requested the Secretariat to revise the draft guidelines in the light of the views expressed during the discussion so as to enable it to adopt appropriate guidelines at its next session. In addition, it was requested that the explanations set forth in paragraphs 4 to 14 of document A/CN.9/189,\* if they were to be used as explanatory notes accompanying the final guidelines, be reformulated for that purpose.

#### *Decision of the Commission*

59. The Commission, at its 248th meeting, on 23 June 1981, adopted the following decision:

#### *The United Nations Commission on International Trade Law*

1. *Decides* that it would be desirable to issue guidelines in the form of recommendations to arbitral institutions and other relevant bodies, such as chambers of commerce, in order to assist them in adopting procedures for their acting as appointing authority or providing administrative services in cases to be conducted under the UNCITRAL Arbitration Rules;

2. *Requests* the Secretary-General to prepare, in the light of the views expressed during the discussion, a further note with a revised text of the draft guidelines and any explanations thereof, and to submit that note to the next session.

#### *B. Model arbitration law<sup>18</sup>*

##### *Introduction*

60. The Commission, at its twelfth session, considered a report of the Secretary-General entitled "Study on the application and interpretation of the Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York, 1958)" (A/CN.9/168)\*\* and a note

by the Secretariat entitled "International commercial arbitration—further work in respect of international commercial arbitration" (A/CN.9/169).<sup>19</sup> The note suggested that the Commission commence work on a model law on arbitral procedure which could help to overcome most of the problems identified in the above study and to reduce the legal obstacles to arbitration.

61. The Commission decided, at that session, to request the Secretary-General:

"(a) To prepare an analytical compilation of provisions of national laws pertaining to arbitration procedures, including a comparison of such laws with the UNCITRAL Arbitration Rules and the 1958 Convention;

"(b) To prepare, in consultation with interested international organizations, in particular the Asian-African Legal Consultative Committee and the International Council for Commercial Arbitration, a preliminary draft of a model law on arbitral procedure, taking into account the conclusions reached by the Commission, and in particular:

"(i) That the scope of application of the draft uniform rules should be restricted to international commercial arbitration;

"(ii) That the draft uniform law should take into account the provisions of the 1958 Convention and of the UNCITRAL Arbitration Rules;

"(c) To submit this compilation and the draft to the Commission at a future session."<sup>20</sup>

62. At its thirteenth session, the Commission had before it a note by the Secretariat entitled "Progress report on the preparation of a model law on arbitral procedure" (A/CN.9/190).<sup>21</sup> In this note, the Secretariat set forth its initial work and referred to difficulties in obtaining the materials necessary for the preparatory work on this project. In order to assist the Secretariat in that regard, the Commission decided to invite Governments to provide the Secretariat with relevant materials on national legislation and case law, and pertinent treaties where available.<sup>22</sup> The General Assembly included a similar appeal to Governments in its resolution 35/51 of 4 December 1980 (para. 12 (d)).

63. The Commission, at its present session, had before it a report of the Secretary-General entitled "Pos-

\* Yearbook . . . 1979, part two, III, D.

<sup>19</sup> Report of the United Nations Commission on International Trade Law on the work of its twelfth session, *Official Records of the General Assembly, Thirty-fourth Session, Supplement No. 17* (A/34/17), paras. 78-80 (Yearbook . . . 1979, part one, II, A).

<sup>20</sup> *Ibid.*, para. 81.

<sup>21</sup> Report of the United Nations Commission on International Trade Law on the work of its thirteenth session, *Official Records of the General Assembly, Thirty-fifth Session, Supplement No. 17* (A/35/17), paras. 114-116 (Yearbook . . . 1980, part one, II, A).

<sup>22</sup> *Ibid.*, para. 117.

\* Yearbook . . . 1980, part two, IV, D.

\*\* Yearbook . . . 1979, part two, III, C.

<sup>18</sup> The Commission considered this subject at its 249th meeting, on 24 June 1981.

sible features of a model law on international commercial arbitration" (A/CN.9/207).<sup>\*</sup> The report, in its first part, deals with the concerns which should be met by the model law and with the principles which could underlie it. In its second part, it attempts to identify all those issues possibly to be dealt with in the draft model law. Those issues relate to the scope of application, the arbitration agreement, the arbitrators, the arbitral procedure, the award, and the means of recourse. The report suggests that the preparation of a model law would be timely and desirable in view of the manifold problems encountered in present arbitration practice and that this work, in view of the complexity of the issues, be entrusted to a Working Group.

#### *Discussion at the session*

64. The Commission took note of the report of the Secretary-General (A/CN.9/207)<sup>\*</sup> and considered the conclusions suggested therein. There was general support for the suggestion to proceed towards the drafting of a model law on international commercial arbitration. This was deemed desirable in view of the manifold problems encountered in present arbitration practice and of the need for a legal framework for equitable and rational settlement procedures for disputes arising out of international trade transactions. It was also stated in support that a model law could be of great value to all States, irrespective of their legal or economic system.

65. The Commission was also agreed that the report setting forth the concerns, purposes and possible contents of a model law would provide a useful basis for the preparation of a model law. While not discussing the issues in detail, the Commission considered the general direction and approach to be taken. It reaffirmed its decision that in preparing the model law due account be taken of the 1958 New York Convention and of the UNCITRAL Arbitration Rules. It was also suggested that every effort be made to take into account the conditions and interests, and meet the needs, of all States, in particular of developing countries. It was important to strike a reasonable balance between the interest of the parties to determine freely the procedure to be followed and the need for mandatory provisions ensuring fair and just proceedings.

66. There was general support for the suggestion that the work of preparing a draft model law be entrusted to a Working Group. It was decided to give that mandate to the Working Group on International Contract Practices which had completed its prior task.

67. Divergent views were expressed as to the desirable size of the Working Group. According to one view, the present composition of the Working Group on Inter-

national Contract Practices (15 States)<sup>23</sup> should be maintained in order to ensure efficient and expeditious work. In support of this view, it was noted that States not members of the Working Group were entitled to attend the sessions as observers and to actively participate in the deliberations pursuant to paragraph 10(c) of General Assembly resolution 31/99 of 15 December 1976. Under another view, the Working Group should be enlarged so as to consist, for example, of 21 States, in order to achieve a wider representation which would enable additional States to participate in view of the great interest in the project. It was noted, in support of this, that regular participation by a State as an observer might be less likely than if it were a member of the Group.

68. The Commission, while recognizing that these issues touched on questions of principle worthy of further consideration, decided to maintain the present size and composition of the Working Group on International Contract Practices. It was agreed that the composition of the Working Group might be re-examined at a future session when the need arose.

69. It was agreed, however, as a matter of principle, that the distribution of memberships in the Working Groups of the Commission should be equitable among the members of the Commission, while maintaining adequate representation of the different regions and of the principal economic and legal systems of the world and of developed and developing countries.

#### *Decision of the Commission*

70. At its 249th meeting, on 24 June 1981, the Commission adopted the following decision:

##### *The United Nations Commission on International Trade Law*

1. *Takes note* of the report of the Secretary-General entitled "Possible features of a model law on international commercial arbitration" (A/CN.9/207);

2. *Decides* to proceed with the work towards the preparation of a draft model law on international commercial arbitration;

3. *Decides* to entrust this work to its Working Group on International Contract Practices with its present composition;

4. *Requests* the Secretary-General to prepare such background studies and draft articles as may be required by the Working Group.

<sup>\*</sup> Reproduced in this volume, part two, III.

<sup>23</sup> The following States are members of the Working Group on International Contract Practices: Austria, Czechoslovakia, France, Ghana, Guatemala, Hungary, India, Japan, Kenya, Philippines, Sierra Leone, Trinidad and Tobago, Union of Soviet Socialist Republics, United Kingdom of Great Britain and Northern Ireland and United States of America.

CHAPTER V. NEW INTERNATIONAL ECONOMIC ORDER<sup>24</sup>*Introduction*

71. The Commission had before it the report of the Working Group on the New International Economic Order on the work of its second session held at Vienna from 9 to 18 June 1981 (A/CN.9/198).<sup>\*</sup> The report sets forth the deliberations of the Working Group on the basis of the study by the Secretary-General entitled "Clauses related to contracts for the supply and construction of large industrial works" (A/CN.9/WG.V/WP.4 and Add.1-8).<sup>\*\*</sup>

72. The report noted that the Working Group had considered 12 out of the 18 chapters of the study and that there still remained some 30 clauses which could be found in contracts for the supply and construction of large industrial works and which yet had to be studied by the Secretariat.

73. The Working Group requested the Secretariat to continue and complete its studies and agreed that the Secretariat should be given discretion in regard to the organization of work, especially in regard to the selection of the additional topics suggested.

74. As regards its future work the Working Group discussed the various options, e.g. legal guide, model clauses, code of conduct, general conditions and conventions. The report noted that there was general agreement that for the time being work should be concentrated on the drafting of a legal guide and it was pointed out that such a guide could well include variants of model clauses whenever appropriate. It was also felt that the preparation of a legal guide would not exclude any further steps at a later stage if this would appear necessary. The formulation of a detailed legal guide covering turn-key and semi-turn-key contracts as well as their variants would be a first practical step in the direction of assisting developing countries in meeting their needs and aspirations. The Working Group entrusted the Secretariat with the drafting of the legal guide.

75. As regards clauses related to industrial co-operation the Working Group considered the note by the Secretariat entitled "Clauses related to industrial co-operation" (A/CN.9/WG.V/WP.5)<sup>\*\*\*</sup> and agreed that work on it be deferred till after the preparation of the legal guide on contractual provisions relating to contracts for the supply and construction of large industrial works.

76. The report also reflected the discussion concerning the next session of the Working Group. The wish was

expressed that the Commission in deciding the dates of the next session should take into account the urgency of the project.

*Discussion at the session*

77. The Commission expressed its appreciation to the Working Group, and its Chairman, Mr. Leif Sevón, for the above manner in which the work had been executed. There was also general agreement that the directions of the future work as decided by the Working Group should be approved. The report of the Working Group was approved.

78. Emphasis was laid on paragraph 14 of the report of the Working Group setting forth the general agreement of the Working Group that its work should be within the context of the basic principles of the new international economic order and in particular should be directed to meeting the needs and aspirations of the developing countries. A view was expressed that not only the needs but also the aspirations and interests of the developing countries should be emphasized.

79. Attention was also directed to paragraph 15 of the report of the Working Group reflecting a view that the work of the Working Group, in view of its mandate, should focus on the aspect of development, especially of developing countries, in order to distinguish this work from the work of other Working Groups of the Commission. Under another view, however, the new international economic order should be looked at as a system which had to be taken into account by all Working Groups of the Commission, and by the Commission as a whole.

80. Observations were made as to the content of the future guide. According to one view the guide should concentrate on those legal problems which the developing countries in particular face in contracts for the supply and construction of large industrial works. Under another view, the transfer of appropriate technology, the continued availability of spare parts and a good after-sales service were especially important for developing countries. The guide, according to this view, should assist enterprises in developing countries in negotiating contracts and identifying unfavourable clauses. In this regard it was observed that the future legal guide would be in the interest not only of developing countries, but also of all parties inexperienced in the negotiation of such contracts.

81. Views were exchanged on the content of a future study on industrial co-operation. It was suggested that such a study, in the light of General Assembly resolution 35/166 and in accordance with the discussion at the first session of the Working Group on the New International Economic Order (A/CN.9/176),<sup>\*</sup> should not only deal with the relations between enterprises but also with inter-

<sup>\*</sup> Reproduced in this volume, part two, IV, A.

<sup>\*\*</sup> Reproduced in this volume, part two, IV, B, 1.

<sup>\*\*\*</sup> Reproduced in this volume, part two, IV, B, 2.

<sup>24</sup> The Commission considered this subject at its 250th meeting, on 24 June 1981.

<sup>\*</sup> Yearbook . . . 1980, part two, V, A.

governmental agreements, as these were of great importance for relations between parties at the enterprise level. This suggestion was supported as well as opposed.

82. The Commission heard statements by the observer from the United Nations Industrial Development Organization (UNIDO) and by the Secretary of the Commission regarding current activities, the overlapping of work, the attempts and possibilities for co-ordination and the necessity for close co-operation between the two organizations. There was general agreement that the Secretariats of UNCITRAL and UNIDO should establish close co-operation. The Commission expressed its appreciation to the observer from UNIDO for his statement indicating the willingness of UNIDO to co-ordinate its work, to the extent possible, with the work of UNCITRAL.

83. While there was general agreement that the work in hand should be executed as expeditiously as possible, views were divided on how quickly the Secretariat and the Working Group should proceed with their work. Under one view the next session of the Working Group should consider the second part of the study by the Secretary-General containing all the remaining topics, and also a sample of the draft legal guide. Another view was that the Secretariat should be given more time to enable it to study all the relevant issues carefully. It was also observed that requesting the Secretariat to prepare studies on all the remaining issues and to draft the legal guide at the same time might overburden the Secretariat. As far as the date of the next session was concerned, it was agreed that this should be decided in the context of the future work of the Commission (see *infra*, chap. IX).

#### *Decision of the Commission*

84. At its 250th meeting, on 24 June 1981, the Commission adopted the following decision:

#### *The United Nations Commission on International Trade Law*

1. *Takes note with appreciation* of the report of the Working Group on the New International Economic Order on the work of its second session and of the study by the Secretary-General entitled "Clauses related to contracts for the supply and construction of large industrial works";

2. *Welcomes and approves* the following decisions of the Working Group concerning its future work:

(a) To request the Secretary-General to continue and complete the study on clauses to be found in contracts for the supply and construction of large industrial works;

(b) To entrust to the Secretary-General the drafting of a legal guide that should identify the legal issues involved in such contracts and suggest possible solu-

tions to assist parties, in particular from developing countries, in their negotiations;

(c) To request the Secretary-General to submit, at a future session, a preliminary study on specific features of industrial co-operation contracts after the preparation of the legal guide on contractual provisions relating to contracts for the supply and construction of large industrial works;

3. *Requests* the Working Group to submit a progress report to the fifteenth session of the Commission.

### CHAPTER VI. CO-ORDINATION OF WORK<sup>25</sup>

#### *Introduction*

85. The Commission had before it General Assembly resolution 2205 (XXI) of 17 December 1966 by which the United Nations Commission on International Trade Law was established and in which the Commission was given the mandate to co-ordinate legal activities in the field of the harmonization and unification of international trade law. The Commission also had before it resolutions 34/42 of 17 December 1979 and 35/51 of 4 December 1980 by which that mandate was re-affirmed.

86. At its thirteenth session in 1980, the Commission was of the view that the co-ordination of the legal activities of United Nations bodies took on a particular importance at a time when those bodies were increasingly active in the elaboration and adoption of legal rules. It was felt that more information was required about the programmes and terms of reference of the various United Nations organs before it would be possible to recommend a concrete course of action.<sup>26</sup>

87. The Commission therefore requested its Secretariat to submit to it at its next annual session complete information on the activities of other organs and international organizations.<sup>27</sup>

88. In response to this request the Commission had before it at its present session a report of the Secretary-General entitled "Current activities of international organizations related to the harmonization and unification of international trade law" (A/CN.9/202 and Add.1-4),\* a report entitled "Question of co-ordination: direction of the work of the Commission" (A/CN.9/

\* Reproduced in this volume, part two, V, A.

<sup>25</sup> The Commission considered this subject at its 246th and 247th meetings, on 22 and 23 June 1981.

<sup>26</sup> Report of the United Nations Commission on International Trade Law on the work of its thirteenth session, *Official Records of the General Assembly, Thirty-fifth Session, Supplement No. 17* (A/35/17), para. 149 (Yearbook . . . 1980, part one, II, A).

<sup>27</sup> *Ibid.*, para. 150.

203)\* and a note by the Secretariat entitled "Co-ordination of activities" (A/CN.9/208).\*\*

89. The Commission was informed that a favourable response had been received by the Secretariat from bodies within and without the United Nations system to the request for information on their current activities relating to international trade law. In addition, representatives from the European Communities and from the secretariats of the Council for Mutual Economic Assistance, the Council of Europe, the Hague Conference on Private International Law (Hague Conference), the International Institute for the Unification of Private Law (UNIDROIT), the Organization of American States (OAS) and the United Nations Industrial Development Organization (UNIDO) made statements to the Commission on the activities of those organizations in the field of international trade law and on the subject of co-ordination of efforts in this field.

90. The Commission was informed that the Hague Conference would convene an extraordinary session in 1985 to revise the 1955 Hague Convention on the Law Applicable to International Sales of Goods. The Hague Conference had decided to invite all States to participate in that session. Non-member States of the Hague Conference would be invited to participate without financial implications as the Government of the Netherlands, and other member States of the Hague Conference, had agreed to make contributions for this purpose.

91. As regards the necessary preparatory work for the revision, the Hague Conference would convene in 1982 a Special Commission to which States members of the Commission that are not members of the Hague Conference would be invited with full capacity. States not members of the Commission could also participate as observers.

92. The Commission was also informed that UNIDROIT had decided to invite States members of the Commission which were not members of UNIDROIT to participate with full capacity in its Committee of Governmental Experts which would consider a draft Uniform Law on Agency of an International Character in the International Sale of Goods. The meeting would be held from 2 to 13 November 1981.

#### *Discussion at the session*

93. The Commission noted with appreciation the various statements from organizations which had expressed their willingness to continue to assist the Commission in its co-ordinating efforts.

94. As regards the decisions taken by the Hague Conference and UNIDROIT to invite members of the

Commission to participate in their preparatory work as noted above, the Commission welcomed these decisions and regarded them as significant steps towards close collaboration in the work of the unification of the law related to international trade. The Commission accordingly recommended to all members of the Commission to participate actively in the preparatory work in response to the invitations.

95. The Commission also expressed its particular appreciation of the report submitted by the International Law Commission on its recent and current activities which might bear upon questions related to the field of international trade law. The suggestion was made that further efforts should be undertaken to strengthen relations between these two Commissions of the General Assembly permanently responsible for legal matters.

96. The view was expressed that care should be taken that the activities of the Commission in respect of contractual provisions relating to contracts for the supply and construction of large industrial works and the efforts of UNIDO in the preparation of model contracts for the construction of fertilizer plants did not result in a duplication of work.

97. It was also suggested that an increased effort should be made to foster co-operation with regional organizations interested in international trade law. Closer contact would reduce the likelihood of a duplication of work and adoption of conflicting regional conventions and could be useful in encouraging the ratification of conventions arising out of the Commission's work. In this regard the need for a global solution was noted, particularly in the field of international shipping legislation. It was also noted that the resolution of the Asian-African Legal Consultative Committee (reproduced as an annex to document A/CN.9/208) recommended to member States of that organization to consider the possibility of ratifying or adhering to the United Nations Convention on the Carriage of Goods by Sea, 1978 (Hamburg), and the United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980). Special mention was also made in this regard of the OAS which had been active in a number of fields of international trade law of interest to the Commission.

98. It was suggested that as a first step the Secretariat should make sure that these organizations received all the relevant documentation in respect of the work of the Commission. However, it was also suggested that to implement adequately the Commission's objective in co-ordinating activities in international trade law, it would be necessary for the Secretariat to establish personal contact with these organizations, particularly by attending their meetings that were devoted to aspects of international trade law. The Commission was of the view that the necessary financial support should be made available for this activity within the framework of existing budgetary resources.

\* Reproduced in this volume, part two, V, B.

\*\* Reproduced in this volume, part two, V, C.



99. At the same time, the Commission expressed the view that it was the duty of Governments represented in various international organizations to exercise control over the programmes of work of those organizations and in particular to ensure that in drawing up those programmes of work, account was taken of existing programmes.

100. The Commission was in agreement that the co-ordination of work in international trade law depended upon the exchange of information. It was noted that the report on current activities of other organizations was useful for ascertaining developments in the field of international trade law. To further strengthen the co-ordinating role of the Commission, it was suggested that, in lieu of the report on current activities in its present form, the Secretariat should select a particular area of international trade law for intensive consideration and submit a report on that area which would focus, *inter alia*, on the following issues: the work of unification already undertaken in that area; parts of that area in which unification had not been undertaken and where unification might appropriately be undertaken; and the most suitable body to undertake the unification. It was understood, however, that this did not preclude the Secretariat from submitting a report on current activities in the present form after a certain interval.

101. The Commission was also of the view that it might, as it had done on some past occasions, endorse where appropriate legal texts emanating from the activities of other organizations active in the field of international trade law.

## CHAPTER VII. TRAINING AND ASSISTANCE IN THE FIELD OF INTERNATIONAL TRADE LAW<sup>28</sup>

### Introduction

102. The Commission, at its thirteenth session, decided to hold the Second UNCITRAL Symposium on International Trade Law on the occasion of its fourteenth session at Vienna. The Commission was informed at the thirteenth session that several States had decided to make contributions for the purpose of awarding fellowships to participants from developing countries to cover their travel and subsistence costs. It invited other States to make similar contributions so that the number of participants from developing countries might be increased.<sup>29</sup>

<sup>28</sup> The Commission considered this subject at its 250th meeting, on 24 June 1981.

<sup>29</sup> Report of the United Nations Commission on International Trade Law on the work of its thirteenth session, *Official Records of the General Assembly, Thirty-fifth Session, Supplement No. 17 (A/35/17)*, para. 162 (Yearbook . . . 1980, part one, II, A).

103. At its current session, the Commission was informed that the Symposium was being held from 22 to 26 June 1981, concurrently with the session of the Commission. Contributions for fellowships had been received from the Governments of Austria, \$US 3,000; Canada, \$US 2,000; Chile, \$US 2,000; Finland, \$US 3,340 (FM 15,000); Italy, \$US 10,000; Netherlands, \$US 9,615 (f. 25,000); Philippines, \$US 1,000; Qatar, \$US 10,000; and Sweden, \$US 2,000. These contributions had permitted the awarding of 15 fellowships to participants from five African States (Central African Republic, Guinea, Liberia, Sudan and Upper Volta); four Asian States (Papua New Guinea, Philippines, Thailand and Yemen Arab Republic); three European States (Malta, Romania and Yugoslavia); and three Latin American States (Argentina, Chile and Honduras). An additional 43 participants from 24 States were attending the Symposium at their own expense.

104. The lectures at the Symposium were given by representatives and observers at the present session and by members of the Secretariat. The Symposium dealt with matters which have been or are on the work programme of the Commission, i.e. the international sale of goods, international payments, carriage of goods by sea, international commercial arbitration and legal aspects of the new international economic order.

105. The Commission was informed that the planning for the Symposium had been greatly hindered by the late payment of pledges. It had not been certain until the final days before the Symposium was held how many fellowships could be awarded. Moreover, some of the pledges had not been received, and, in several cases, it had been necessary to withdraw the expected award of a fellowship because the funds were not available at the necessary time.

106. In respect of regional seminars, at its thirteenth session, the Commission requested the Secretary-General to "report to it on the possibility of holding regional seminars".<sup>30</sup> In response to that request, the Commission had before it a report of the Secretary-General entitled "Training and assistance: possibility of holding regional seminars" (A/CN.9/206).<sup>\*</sup> This report discussed some of the administrative considerations which would be involved in a decision to hold regional seminars.

107. The Commission was also informed that the Secretariat had been in contact with several regional organizations to inquire whether seminars on international trade law might be organized on the occasion of their annual sessions. The Secretary-General of the Asian-African Legal Consultative Committee had expressed an interest if the host Government to the Committee's annual meeting would be willing to assume the local costs of such a seminar. Furthermore, several bar

<sup>\*</sup> Reproduced in this volume, part two, VII.

<sup>30</sup> *Idem*.

associations had indicated willingness to furnish lecturers for such seminars. The activities of the Organization of American States in sponsoring seminars, and the activities of the Council for Mutual Economic Assistance in awarding fellowships to candidates from developing countries, were also mentioned.

#### *Discussion at the session*

108. The Commission expressed its appreciation to those States which had contributed to fellowships for participants from developing countries. It also expressed its appreciation to those representatives and observers who had given lectures.

109. There was agreement that the Commission should continue to sponsor symposia and seminars on international trade law. It was considered desirable for these seminars to be organized on a regional basis. In this way, it was felt, a larger number of participants from the region could attend and the seminars would themselves help to promote the adoption of the texts emanating from the work of the Commission. The Commission welcomed the possibility that regional seminars might be sponsored jointly with regional organizations. The Secretariat was requested to make such arrangements as it found desirable in this regard.

110. The Commission noted the serious problems caused by the uncertain financial resources available for the Commission's programme in training and assistance and the administrative difficulties caused by the late payment of pledges. It expressed the hope that States would once again make contributions for the purposes of the Commission's programme of training and assistance.

111. The Commission requested the Secretariat to continue its efforts to bring about the holding of regional seminars.

### CHAPTER VIII. STATUS OF CONVENTIONS<sup>31</sup>

#### *Introduction*

112. At its twelfth session, the Commission decided that the agenda of future sessions should include as an item the exchange of views on the state of signatures, ratifications and accessions to conventions based on drafts prepared by the Commission.<sup>32</sup> The Commission

had before it a note by the Secretariat entitled "Status of Conventions" (A/CN.9/205).<sup>33</sup>

#### *Discussion at the session*

113. An exchange of views took place among representatives on their expectations as to the likely actions of their States as regards signing, ratifying or acceding to these conventions. It was noted that, while as regards some States these likely actions, and the time periods in which they might occur, could be predicted with some certainty, as regards other States necessary governmental formalities precluded a definite prediction. The discussion revealed, however, a definite trend towards a wider acceptance of the conventions in the next two or three years. It was recognized that the exchange of views served a useful function, as many States, in deciding on their own future action, took into account the intended action of other States.

114. There was wide agreement, however, that more effective action than an exchange of views was necessary to promote wider acceptance of the conventions. A suggestion was made that the Commission should communicate with all States, bringing to their notice the conventions, together with information regarding their possible entry into force, and appealing to them to sign, ratify or accede to the conventions. In reply, it was noted that a communication by the Commission recommending conventions which were the results of its own work might be injudicious. Furthermore, States might be reluctant to enter into communications with the Commission involving their reasons for not ratifying or acceding to these conventions.

115. The Commission took note of the note by the Secretariat entitled "Co-ordination of activities" (A/CN.9/208)\*\* which showed that the Asian-African Legal Consultative Committee had recommended to the Governments of member States to consider the possibility of ratifying or adhering to the United Nations Convention on the Carriage of Goods by Sea, 1978 (Hamburg), and the United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980). There was general agreement that the Secretariat should be encouraged to utilize various opportunities including contacts with regional bodies with a view to promoting the Conventions.

116. The Secretary of the Commission stated that a possible course might be for the Commission to recommend to the General Assembly that it authorize the Secretary-General to bring these Conventions to the notice of all States which have not ratified or acceded to

<sup>31</sup> The Commission considered this subject at its 245th meeting, on 22 June 1981.

<sup>32</sup> Report of the United Nations Commission on International Trade Law on the work of its twelfth session, *Official Records of the General Assembly, Thirty-fourth Session, Supplement No. 17* (A/34/17), para. 132 (Yearbook . . . 1979, part one, II, A).

\* See A/CN.9/205/Rev.1, reproduced in this volume, part two, VI.

\*\* Reproduced in this volume, part two, V, C.

<sup>33</sup> A/CN.9/205 has now been issued as A/CN.9/205/Rev.1 in order to incorporate relevant information received during the fourteenth session of the Commission.



them, together with information as to the mode of their entry into force and the current status of ratifications and accessions, and accompanied by an invitation to be answered within a specified period of time to supply him with information on the steps that have been taken with regard to ratification or accession. It was decided to adopt this course.

117. It was also decided that the Secretariat should inform the Commission at its next session of the result of the above inquiry together with a report on the status of the Conventions.

#### *Decision of the Commission*

118. At its 245th meeting, on 22 June 1981, the Commission adopted the following decision:

#### *The United Nations Commission on International Trade Law,*

Recognizing the value for the unification of international trade law of the entry into force at an early date, and the wide acceptance, of the Convention on the Limitation Period in the International Sale of Goods (New York, 1974); the Protocol amending the Convention on the Limitation Period in the International Sale of Goods (Vienna, 1980); the United Nations Convention on the Carriage of Goods by Sea, 1978 (Hamburg); and the United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980),

Being of the opinion that the General Assembly is the most appropriate body to initiate action directed to these ends;

1. *Recommends* to the General Assembly that it authorize the Secretary-General:

(a) To bring these Conventions to the notice of all States which have not ratified or acceded to them, and to communicate to them information as to the mode of their entry into force and the current status of ratifications and accessions;

(b) To invite States within a specified period of time to supply him with information on the steps that have been taken with regard to ratification or accession;

2. *Requests* the Secretariat to take such measures as it deems appropriate to promote the wider acceptance of these Conventions.

#### CHAPTER IX. FUTURE WORK AND OTHER BUSINESS<sup>34</sup>

##### *A. Medium-term plan of the Commission*

119. The Commission had before it a draft medium-term plan of the Commission for the years 1984-1989 as drafted by the Secretariat (A/CN.9/XIV/R.1).

<sup>34</sup> The Commission considered this subject at its 250th meeting, on 24 June 1981.

120. In accordance with General Assembly resolution 34/224 of 20 December 1979, the Commission reviewed this draft plan.

121. The text of paragraph 12 of the draft plan commenced as follows:

#### *"Strategy of the Secretariat:*

"12. This will involve the following continuing activities:

undertaking the research, drafting and documentation (where necessary with assistance from consultants) required by UNCITRAL or its Working Groups or necessary for Diplomatic Conferences;

...."

122. The Commission deleted the words in parenthesis quoted above and, subject to this modification, approved the medium-term plan. The Commission was of the view that this deletion did not affect the use of consultants by the Secretariat in accordance with the normal United Nations practice.

123. The Commission was of the view that, at the present stage, the plan did not contain any activities which may be considered as obsolete, of marginal usefulness or ineffective. The Commission also considered that the subprogrammes set forth therein should be given equal priority.

#### *B. General Assembly resolutions*

##### *(i) General Assembly resolution on international economic law*

124. The Commission took note of General Assembly resolution 35/166 of 15 December 1980 in which the Commission was requested to submit relevant information to, and to co-operate fully with, the United Nations Institute for Training and Research (UNITAR) in its study on the existing and evolving principles and norms of international law relating to the new international economic order concerning the economic relations among States, international organizations, other entities of public international law, and the activities of transnational corporations.

125. The Secretary informed the Commission that the Secretariat had submitted relevant information concerning the activities of the Commission in the field of the new international economic order to UNITAR.

##### *(ii) General Assembly resolution on summary records of the Commission*

126. The Commission took note with appreciation of General Assembly resolution 35/51 of 4 December 1980 by which the Commission was authorized to have summary records for its sessions devoted to the preparation of draft conventions and other legal instruments.

(iii) *General Assembly resolution on the work of the Commission*

127. The Commission took note with appreciation of General Assembly resolutions 35/51 of 4 December 1980 on the report of the United Nations Commission on International Trade Law on the work of its thirteenth session and 35/52 of 4 December 1980 on the UNCITRAL Conciliation Rules.

C. *Date of the fifteenth session of the Commission*

128. It was decided that the fifteenth session of the Commission would be held from 26 July to 6 August 1982 in New York.

D. *Sessions of the Working Groups*

129. It was decided that the twelfth session of the Working Group on International Negotiable Instruments would be held in January 1982 at Vienna.

130. As regards the next session of the Working Group on International Contract Practices, it was noted that the accepted pattern of alternation of the location of the session between New York and Vienna would call for the next session to be held at Vienna, and the session after that to be held in New York. It was also noted that no session of the Working Group could be held in New York in the autumn of 1982 because of the holding of the

thirty-seventh session of the General Assembly. In order not to foreclose the possibility of holding two sessions of the Working Group in 1982 to expedite the work, it was agreed that the third session of the Working Group on International Contract Practices would be held from 16 to 26 February 1982 in New York. This would permit the holding of a further session in the autumn of 1982 at Vienna. However, it was also agreed that the need for a further session of the Working Group in 1982 would be decided at the next session of the Commission.

131. It was decided that the third session of the Working Group on the New International Economic Order would be held from 12 to 23 July 1982 in New York.

E. *Composition of the Commission*

132. The observer of the People's Republic of China drew the attention of the Commission to the fact that his country had actively participated in the work of the Commission in recent years. He stated that his country now wished to become a member of the Commission when its composition was next renewed.

ANNEX

List of documents before the Commission

[Annex not reproduced. See check list of UNCITRAL documents at the end of this volume.]

**B. United Nations Conference on Trade and Development (UNCTAD): extract from the report of the Trade and Development Board (twenty-third session)\***

*"B. Progressive development of the law of international trade: fourteenth annual report of the United Nations Commission on International Trade Law (agenda item 10 (b))*

"526. For the consideration of this item the Board had before it the report of UNCITRAL on the work of its fourteenth session,<sup>31</sup> circulated under cover of TD/B/868.

*"Action by the Board*

"527. At its 556th meeting, on 29 September 1981, the Board took note of the report of UNCITRAL on its fourteenth session.

<sup>31</sup> For the printed text, see *Official Records of the General Assembly, Thirty-sixth Session, Supplement No. 17 (A/36/17)* (reproduced in this volume, part one, A).

\* *Official Records of the General Assembly, Thirty-sixth Session, Supplement No. 15 (A/36/15)*, vol. II, chapter VII: Other matters in the field of trade and development.

### C. General Assembly: report of the Sixth Committee (A/36/669)\*

1. On the recommendation of the General Committee, the General Assembly decided at its 4th plenary meeting, on 18 September 1981, to include in the agenda of its thirty-sixth session the item entitled "Report of the United Nations Commission on International Trade Law on the work of its fourteenth session" and to allocate it to the Sixth Committee.

2. In connexion with this item, the Sixth Committee had before it the report in question, which was introduced by the Chairman of the United Nations Commission on International Trade Law at the 3rd meeting of the Committee, on 23 September.<sup>1</sup> In addition to that report, the Committee had before it a note by the Secretary-General (A/C.6/36/L.6) relating to the consideration of the report by the Trade and Development Board of the United Nations Conference on Trade and Development.

3. The Sixth Committee considered the item at its 3rd to 7th meetings, from 23 September to 29 September,

and at its 42nd meeting, on 6 November 1981. The summary records of those meetings (A/C.6/36/SR.3-7 and 42) contain the views of representatives who spoke during the consideration of the item.

4. The Committee also had before it a draft resolution (A/C.6/36/L.7), which was introduced by the representative of Austria at the 42nd meeting, on 6 November, sponsored by Argentina, Australia, Austria, Brazil, Canada, Chile, Cyprus, Czechoslovakia, Egypt, Finland, France, Germany, Federal Republic of, Greece, Hungary, India, Italy, Jamaica, Japan, Kenya, Mongolia, Morocco, the Netherlands, Nigeria, the Philippines, Romania, Spain, Sweden, Turkey and Yugoslavia, later joined by Bolivia, Senegal, Singapore, Thailand, Trinidad and Tobago and Zaire.

5. At the same meeting, the Committee adopted draft resolution A/C.6/36/L.7 by consensus (see para. 6).

#### RECOMMENDATION OF THE SIXTH COMMITTEE

6. The Sixth Committee recommends to the General Assembly the adoption of the following draft resolution:

*[Text not reproduced in this section. The draft resolution was adopted, with editorial changes, as General Assembly resolution 36/32. See section D, below.]*

### D. General Assembly resolution 36/32 of 13 November 1981

#### 36/32. REPORT OF THE UNITED NATIONS COMMISSION ON INTERNATIONAL TRADE LAW

*The General Assembly,*

*Having considered* the report of the United Nations Commission on International Trade Law on the work of its fourteenth session,<sup>1</sup>

*Recalling* that the object of the United Nations Commission on International Trade Law is the promotion of the progressive harmonization and unification of international trade law,

*Recalling*, in this regard, its resolution 2205 (XXI) of 17 December 1966, by which it established the United Nations Commission on International Trade Law and defined the object and terms of reference of the Commission, 3108 (XXVIII) of 12 December 1973, by which it increased the membership of the Commission, 31/99 of 15 December 1976, by which Governments of Member States not members of the Commission were entitled to

attend the sessions of the Commission and its Working Groups as observers, and 34/142 of 17 December 1979, by which the co-ordinating function of the Commission in the field of international trade law was emphasized, as well as its previous resolutions concerning the reports of the Commission on the work of its annual sessions,

*Recalling also* its resolutions 3201 (S-VI) and 3202 (S-VI) of 1 May 1974, 3281 (XXIX) of 12 December 1974 and 3362 (S-VII) of 16 September 1975,

*Reaffirming* its conviction that the progressive harmonization and unification of international trade law, in reducing or removing legal obstacles to the flow of international trade, especially those affecting the developing countries, would significantly contribute to universal economic co-operation among all States on a basis of equality, equity and common interests and to the elimination of discrimination in international trade and, thereby, to the well-being of all peoples,

*Having regard* for the need to take into account the different social and legal systems in harmonizing the rules of international trade law,

\* 11 November 1981, *Official Records of the General Assembly, Thirty-sixth Session*, agenda item 117.

<sup>1</sup> *Official Records of the General Assembly, Thirty-sixth Session, Supplement No. 17 (A/36/17)* (reproduced in this volume, part one, A). The presentation of the report was pursuant to a decision by the Sixth Committee at its 1096th meeting, on 13 December 1968 (see *Official Records of the General Assembly, Twenty-third Session, Annexes*, agenda item 88, document A/7408, para. 3) (Yearbook . . . 1968-1970, part two, I, B, 2).

<sup>1</sup> *Official Records of the General Assembly, Thirty-sixth Session, Supplement No. 17 (A/36/17)* (reproduced in this volume, part one, A).

## I. INTERNATIONAL CONTRACT PRACTICES\*

### A. Report of the Working Group on International Contract Practices on the work of its second session (New York, 13-17 April 1981) (A/CN.9/197)\*\*

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\* For consideration by the Commission see Report, chapter III (part one, A, above).

\*\* 8 May 1981. Referred to in Report, para. 38 (part one, A, above). See also Note by the Secretariat: alternative methods for the final adoption of conventions emanating from the work of the Commission (A/CN.9/204), reproduced in this volume, part two, VIII.

#### Introduction

1. At its twelfth session, the United Nations Commission on International Trade Law decided that work should be undertaken directed to the formulation of uniform rules regulating liquidated damages and penalty clauses, and that the work should be entrusted to the Working Group on International Contract Practices, and requested the Working Group to consider the feasibility of formulating uniform rules on liquidated damages and penalty clauses applicable to a wide range of international trade contracts.<sup>1</sup>

2. The Working Group is currently composed of the following States members of the Commission: Austria, Czechoslovakia, France, Ghana, Guatemala, Hungary, India, Japan, Kenya, Philippines, Sierra Leone, Trinidad and Tobago, Union of Soviet Socialist Republics, United Kingdom of Great Britain and Northern Ireland and United States of America.

3. The Working Group held its first session at Vienna, from 24 to 28 September 1979. At the conclusion of that session the Working Group decided that further work by the Working Group on the subject of liquidated damages and penalty clauses was justified, and recom-

mended to the Commission the holding of a further session of the Working Group.<sup>2</sup> This recommendation was adopted by the Commission at its thirteenth session.<sup>3</sup>

4. The Working Group held its second session at United Nations Headquarters from 13 to 17 April 1981. All the members of the Working Group were represented except Ghana, Guatemala and Sierra Leone.

5. The session was attended by observers from the following States members of the Commission: Australia, Cuba, German Democratic Republic, Nigeria and Yugoslavia.

6. The session was also attended by observers from the following Member States of the United Nations: Canada, El Salvador, Gabon, Greece, Malaysia, Niger, Thailand and Uruguay.

7. The session was attended by an observer from the following United Nations organ: United Nations Industrial Development Organization.

8. The session was attended by an observer from the following international non-governmental organization: International Chamber of Commerce.

<sup>1</sup> Report of the United Nations Commission on International Trade Law on the work of its twelfth session (1979), *Official Records of the General Assembly, Thirty-fourth Session, Supplement No. 17* (A/34/17), para. 31 (Yearbook . . . 1979, part one, II, A).

<sup>2</sup> Report of the Working Group on the work of its first session (A/CN.9/177, para. 43) (Yearbook . . . 1980, part two, II).

<sup>3</sup> Report of the United Nations Commission on International Trade Law on the work of its thirteenth session (1980), *Official Records of the General Assembly, Thirty-fifth Session, Supplement No. 17* (A/35/17), para. 16 (Yearbook . . . 1980, part one, II, A).

9. The Working Group elected the following officers:

Chairman: ..... Mr. I. Tarko (Austria)  
Rapporteur: ..... Mr. M. Cuker (Czechoslovakia)

10. The following documents were placed before the Working Group:

(a) Report of the Secretary-General entitled "Liquidated damages and penalty clauses (I)" (A/CN.9/161);\*

(b) Report of the Working Group on International Contract Practices on the work of its first session (A/CN.9/177);\*\*

(c) Report of the Secretary-General entitled "Liquidated damages and penalty clauses (II)" (A/CN.9/WG.2/WP.33 and Add.1);\*\*\*

(d) Provisional agenda for the session (A/CN.9/WG.2/WP.32).

11. The Working Group adopted the following agenda:

(a) Election of officers.

(b) Adoption of the agenda.

(c) Consideration of the feasibility of formulating uniform rules on liquidated damages and penalty clauses applicable to a wide range of international trade contracts.

(d) Other business.

(e) Adoption of the report.

#### Consideration of revised draft rules submitted by the Secretariat

12. The Working Group decided to examine the revised draft rules on liquidated damages and penalty clauses submitted by the Secretariat.<sup>4</sup>

#### SCOPE OF APPLICATION

##### *Revised draft rule 1*

13. Revised draft rule 1 as considered by the Working Group is as follows:

"These rules apply to a contract in which the parties have agreed [in writing] that, upon a total or partial failure of performance by a party (the debtor), another party (the creditor) is entitled to recover, or to forfeit, an agreed sum of money."

14. The Working Group was of the view that the formulation of this draft rule would depend on a decision to be taken as to the form the uniform rules might take

(convention, model law or model clauses). Accordingly, the Working Group decided to defer consideration of revised draft rule 1 until the conclusion of its deliberations on the other draft rules.

#### REGULATION OF THE CONTRACT BY THE RULES

##### *Revised draft rule 2*

15. Revised draft rule 2 as considered by the Working Group is as follows:

"Unless the parties have agreed otherwise, the creditor is not entitled to recovery or forfeiture of the agreed sum if the debtor is not liable for the failure of performance."

16. The Working Group adopted revised draft rule 2.

17. It was decided that in the English version of the rules, the terms "creditor" and "debtor" should be replaced by the terms "obligee" and "obligor" respectively.

18. One representative expressed the view that the phrase "not liable for the failure of performance" needed clarification.

##### *Revised draft rule 3*

19. Revised draft rule 3 as considered by the Working Group is as follows:

"1. When the agreed sum is intended by the parties to be complete compensation for the loss caused by a failure of performance, the creditor cannot enforce performance if he enforces recovery or forfeiture, of the agreed sum.

"2. When the agreed sum is intended by the parties to compensate the creditor for the loss caused in the period between a failure of performance and the time when proper performance is rendered, the creditor may enforce performance, and also enforce recovery, or forfeiture, of the agreed sum.

"3. Parties may by agreement provide otherwise."

20. There was wide agreement that the reference to the intention of the parties in the formulation of paragraphs (1) and (2) was undesirable. There was uncertainty as to the criteria for determining the intention of the parties, and furthermore in the case of certain contracts, the intention of the parties may not be ascertainable from the contracts. A formulation referring only to the agreement of the parties was preferable.

21. The view was expressed that both paragraphs (1) and (2) implied that in certain circumstances the obligee was entitled to enforce performance. However, under some legal systems the remedy of enforcement of performance was not normally available. It was agreed that

\* Yearbook . . . 1979, part two, I, C.

\*\* Yearbook . . . 1980, part two, II.

\*\*\* Reproduced in this volume, part two, I, B, 1 and 2.

<sup>4</sup> The revised draft rules are set forth in document A/CN.9/WG.2/WP.33, Part IV (reproduced in this volume, part two, I, B, 1).

there should be clarification that enforcement of performance was available only when the applicable legal system granted such enforcement.

22. It was suggested that the issue of the combination of possible remedies dealt with by this revised draft rule might be resolved by reference to the distinction between total and partial failure of performance. In case of total failure, the obligee should only be entitled to enforce either performance of the main obligation or recovery of the agreed sum. In case of partial failure, the obligee should be entitled to enforce both performance and recovery of the agreed sum. It was noted, however, that in certain cases there may be difficulty in distinguishing between total and partial performance.

23. It was observed that it would be preferable not to use the term compensation in this revised draft rule. The relationship between the right to compensation and the right to the agreed sum was regulated, not in this draft rule, but in draft rule 5.

24. After deliberation, the Working Group requested the Secretariat to submit two alternative re-drafts of revised draft rule 3 on the following lines. The first alternative should set forth as a main rule that the obligee was entitled both to performance and recovery of the agreed sum, save in exceptional cases to be specified. The second alternative should set forth as a main rule that the obligee was only entitled either to performance or to recovery of the agreed sum, save in exceptional cases to be specified.

25. The Secretariat submitted to the Working Group the following alternatives:

#### *Alternative A*

"1. By claiming the agreed sum, the obligee does not lose his right to performance, unless:

"(a) The parties have agreed otherwise, or

"(b) He recovers the agreed sum which can reasonably be regarded as a substitute for performance.

"2. By claiming performance, the obligee does not lose his right to the agreed sum, unless:

"(a) The parties have agreed otherwise, or

"(b) He obtains performance, and the agreed sum can reasonably be regarded as a substitute for performance."

#### *Alternative B*

"By recovering the agreed sum, the obligee loses his right to performance, and by obtaining performance, the obligee loses his right to the agreed sum, unless:

"(a) The parties have agreed otherwise, or

"(b) The agreed sum cannot reasonably be regarded as a substitute for performance."

26. Support was expressed for each of the above alternatives. In support of alternative A, it was noted that in international contract practice, liquidated damages and penalties were most often provided for delay in performance, and that the main rule provided in this alternative was the rule generally applied in such cases. It was also noted that the main rule in this alternative supported the right to obtain performance, which was the principal right under a contract.

27. In support of alternative B, it was noted that this led to results which were fair to both parties.

28. It was observed that the significant difference between the two alternatives was in the different allocation of the burden of proof between the obligor and obligee.

29. During the consideration of the above two alternatives, one representative submitted the text of a proposed draft rule 3 to the Working Group, and this text was referred by the Working Group for consideration by a drafting party. The draft of the drafting party was adopted by the Working Group subject to a minor modification, and is as follows:

"1. Where the agreed sum is recoverable, or subject to forfeiture, on delay in performance of the obligation, the obligee is entitled to both performance of the obligation and the agreed sum.

"2. Where the agreed sum is recoverable, or subject to forfeiture, on non-performance, or defective performance other than delay, the obligee can obtain either performance, or recovery or forfeiture of the agreed sum, unless the agreed sum cannot reasonably be regarded as a substitute for performance.

"3. The rules set forth above shall not prejudice any contrary agreement made by the parties."

30. One representative observed that cases had occurred where contracts provided for the payment of agreed sums for non-acceptance of goods. Suppliers had then concentrated their deliveries so that it was physically impossible for the buyers to accept the goods, and thereafter had sought to recover the agreed sums. It was stated in reply that this difficulty might be resolved under proposed draft rule 6 dealing with the reduction of the agreed sum, or by reference to draft rule 2, under which the buyer may not be liable for non-acceptance in such circumstances.

#### *Revised draft rule 5*

31. Revised draft rule 5 as considered by the Working Group is as follows:

"If a failure of performance in respect of which parties have agreed that a sum of money is to be recoverable, or forfeited, occurs, the creditor is only entitled to recover, or forfeit, the sum, and is not entitled to damages. Parties may agree that the creditor, if he

proves that his loss exceeds the amount of such sum, may also recover the amount of the excess."

32. The Working Group was of the view that parties should be given the power to modify any aspect of the rule by agreement.

33. Opinion was divided on the merits of the draft rule. The view was expressed that it would be preferable to delete the second sentence of the rule, because such a deletion would simplify the rule and reduce the prospects of litigation. On the other hand, it was stated that fairness to the creditor required that he be entitled, where his loss exceeded the agreed sum, to recover in addition to the agreed sum, damages in the amount of such excess, irrespective of an agreement between the parties. According to one view, this was the rule prevalent in current international contract practice.

34. After deliberation, the Working Group requested the Secretariat to submit to the Working Group alternative drafts reflecting the different views expressed.

35. The Secretariat submitted the following alternative drafts:

#### *Alternative A*

"Unless the parties have agreed otherwise, if a failure of performance in respect of which the parties have agreed that a sum of money is to be recoverable, or forfeited, occurs, the creditor is entitled to recover, or forfeit, the sum and is not entitled to damages."

#### *Alternative B*

"Unless the parties have agreed otherwise, if a failure of performance in respect of which the parties have agreed that a sum of money is to be recoverable, or forfeited, occurs, the creditor is entitled to recover, or forfeit the sum and is entitled to damages to the extent that he proves that his loss exceeds the agreed sum."

36. Support was expressed for each of the above alternatives for the reasons set forth in paragraph 33 above.

37. The view was also expressed that, in certain situations, there was uncertainty when alternative A above was considered in relation to draft rule 3. Under draft rule 3, the creditor who chose to enforce performance might lose his right to the agreed sum. If, for any reason, he then failed to obtain performance, he may be left with no remedy, as alternative A above excluded his right to damages. It was proposed that the difficulty might be resolved by adding in alternative A the words "in respect of this failure" after the word "entitled", and the Working Group adopted this proposal. It was noted that if alternative B was adopted, the same modification should be made.

38. It was observed that the appropriate rule to be adopted under draft rule 5 might depend on a decision on

the rule to be adopted in draft rule 6 regulating the possible variation of the agreed sum, and the Working Group accordingly considered revised draft rule 6, without taking a final decision on the formulation of draft rule 5.

#### *Revised draft rule 6*

39. Revised draft rule 6 as considered by the Working Group is as follows:

##### *Variant 1*

"The agreed sum shall neither be increased nor reduced."

##### *Variant 2*

"The agreed sum specified may be reduced when it is [manifestly] [grossly] excessive [in relation to the loss which has occurred], but only if such sum did not constitute a genuine pre-estimate by the parties of the loss likely to be suffered by the creditor."

##### *Variant 3*

"An agreement of the kind described in Rule 1 above shall be void if the agreed sum is [manifestly] [grossly] excessive in relationship to both (a) the loss that could reasonably have been anticipated from the failure of performance, and (b) the actual loss caused thereby. The agreement shall not be void if the loss could not have been precisely predicted or cannot be precisely established."

40. There was little support for variant 1 as an exclusive rule. However, it was proposed that the principle stated in variant 1 might be combined with some of the rules contained in variant 2 to produce an acceptable result. Accordingly, the Working Group requested the Secretariat to submit an alternative draft of rule 6. Combining the two variants, the Secretariat submitted the following alternative draft on the assumption that alternative A of the Secretariat draft of rule 5 (para. 35 above) would be adopted.

"1. The agreed sum shall neither be increased nor reduced.

"2. However, the agreed sum may either be increased or reduced if it is grossly disproportionate in relation to the loss which has occurred.

"[3. The rule in paragraph 2 may be invoked only in cases where the agreed sum cannot reasonably be regarded as a genuine pre-estimate by the parties of the loss likely to be suffered by the obligee.]"

41. It was observed that paragraph 2 of this draft made the increase and reduction of the agreed sum dependent on the same condition. However, in relation to increase, account had to be taken of the consideration that the agreed sum was often intended to be a limitation on liability, and therefore not intended to be subject to



increase. Increase and decrease should therefore be treated differently. It was also suggested that the disproportion referred to in paragraph 2 should be judged, not by relating the agreed sum to the loss which had occurred, but by relating it to a genuine and reasonable pre-estimate to be made at the time of concluding the contract.

42. The Secretariat therefore submitted a further draft of rules 5 and 6, taking into account the deliberations in the Working Group. This draft was adopted by the Working Group, subject to certain modifications, and is as follows:

#### *Rule 5*

"Unless the parties have agreed otherwise, if a failure of performance in respect of which the parties have agreed that a sum of money is to be recoverable or forfeited occurs, the creditor is entitled, in respect of the failure, to recover or forfeit the sum, and is entitled to damages to the extent of the loss not covered by the agreed sum, but only if he can prove that his loss grossly exceeds the agreed sum."

#### *Rule 6*

"(1) The agreed sum shall not be reduced by a court or arbitral tribunal.

"(2) However, the agreed sum may be reduced if it is shown to be grossly disproportionate in relation to the loss that has been suffered by the obligee, and if the agreed sum cannot reasonably be regarded as a genuine pre-estimate by the parties of the loss likely to be suffered by the obligee."

43. It was noted that where parties had agreed that the specified sum was to serve as a limitation of liability, the opening phrase of rule 5 ("unless the parties have agreed otherwise,") would prevent the recovery of damages in addition to the agreed sum. However, two representatives expressed the view that this opening phrase might not achieve this result, and that the rule might produce unexpected results, and that a different wording was required.

44. It was noted that in the French version of these rules the word "grossly" should be rendered by the word "manifestement".

### SCOPE OF APPLICATION

#### *Revised draft rule 1*

45. After concluding its deliberations on draft rules 2 to 6, the Working Group resumed its consideration of draft rule 1 and considered the form that the uniform rules might take.

46. The Working Group decided that the issue of

form should be left for decision by the Commission. In this connexion, the Secretary of the Commission stated that the Secretariat would place before the fourteenth session of the Commission a study examining the range of possible approaches which the Commission might undertake, and that the issue of the form of the rules might be decided after a consideration of that study. One representative stated that the business community in his country was of the view that it would not be useful to cast the uniform rules in the form of rules of law.

47. The Working Group noted that the present formulation of draft rule 1 did not deal with (a) definition of the circumstances which would make a contract qualify as international; and (b) whether any types of contract are to be excluded from the scope of the rules and if so, how this should be done.

48. The Working Group was of the view that, if the rules were to take the form of a convention, some additional provisions would be required to resolve these issues in an appropriate manner. The Secretariat might be requested to draft such additional rules.

49. The question was raised as to the scope of the entitlement to forfeit an agreed sum of money given to the obligee under draft rule 1, and referred to in the other draft rules. It was noted in reply that the entitlement to forfeit included rights given to the obligee by agreement with the obligor in the following cases:

(a) It is agreed between the parties that a sum of money paid by the obligor to the obligee is to be retained (forfeited) by the obligee in the event of failure of performance by the obligor, but returned in the event of proper performance;

(b) It is agreed between the parties that a sum of money due from the obligee to the obligor is to be withheld (forfeited) by the obligee in the event of failure of performance by the obligor, but paid in the event of proper performance.

50. The Working Group provisionally adopted revised draft rule 1, subject to certain modifications, and the draft rule as modified is as follows:

"These rules apply to an international contract in which the parties have agreed [in writing] that, upon a total or partial failure of performance by a party (the obligor), another party (the obligee) is entitled to recover, or to forfeit, an agreed sum of money."

### Other matters

51. The Working Group requested the Secretariat to examine the draft rules adopted by the Working Group to ensure consistency in terminology, and to reproduce in an annex to this report the text of the draft rules as revised.



## ANNEX

Draft rules on liquidated damages and penalty clauses  
adopted by the Working Group<sup>a</sup>

## SCOPE OF APPLICATION

## Draft rule 1

"These rules apply to an international contract in which the parties have agreed [in writing] that, upon a total or partial failure of performance by a party (the obligor), another party (the obligee) is entitled to recover, or to forfeit, an agreed sum of money."<sup>b</sup>

## Draft rule 2

"Unless the parties have agreed otherwise, the obligee is not entitled to recover or to forfeit the agreed sum if the obligor is not liable for the failure of performance."

## REGULATION OF THE CONTRACT BY THE RULES

## Draft rule 3

"1. Where the agreed sum is to be recoverable or forfeited on delay in performance of the obligation, the obligee is entitled to both performance of the obligation and the agreed sum.

"2. Where the agreed sum is to be recoverable or forfeited on non-performance, or defective performance other than delay, the obligee is

<sup>a</sup> Changes have been made in the text of draft rules 2, 3 and 4 to ensure consistency in terminology.

<sup>b</sup> For additional provisions which might be required, see para. 48 above.

entitled either to performance, or to recover or forfeit the agreed sum, unless the agreed sum cannot reasonably be regarded as a substitute for performance.

"3. The rules set forth above shall not prejudice any contrary agreement made by the parties."

Draft rule 5<sup>c</sup>

"Unless the parties have agreed otherwise, if a failure of performance in respect of which the parties have agreed that a sum of money is to be recoverable or forfeited occurs, the obligee is entitled, in respect of the failure, to recover or forfeit the sum, and is entitled to damages to the extent of the loss not covered by the agreed sum, but only if he can prove that his loss grossly exceeds the agreed sum."

## Draft rule 6

"1. The agreed sum shall not be reduced by a court or arbitral tribunal.

"2. However, the agreed sum may be reduced if it is shown to be grossly disproportionate in relation to the loss that has been suffered by the obligee, and if the agreed sum cannot reasonably be regarded as a genuine pre-estimate by the parties of the loss likely to be suffered by the obligee."

<sup>c</sup> Draft rule 4 submitted by the Secretariat to the first session of the Working Group was deleted by the Working Group at that session. No rule 4 was included in the revised draft rules submitted to the second session of the Working Group. In order to facilitate comparison with the draft rules submitted to the first session, the numbering of revised draft rules 5 and 6, which correspond to draft rules 5 and 6 submitted to the first session, have been retained.

B. Working Paper submitted to the Working Group on International Contract Practices  
at its second session (New York, 13-17 April 1981)

## 1. REPORT OF THE SECRETARY-GENERAL: LIQUIDATED DAMAGES AND PENALTY CLAUSES (II) (A/CN.9/WG.2/WP.33)\*

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\* 12 February 1981.

## Introduction

1. At its twelfth session (1979) the United Nations Commission on International Trade Law requested its Working Group on International Contract Practices to consider the feasibility of formulating uniform rules on liquidated damages and penalty clauses applicable to a wide range of international trade contracts.<sup>1</sup>

2. Pursuant to this request, the Working Group held its first session at Vienna (24-28 September 1979).<sup>2</sup> At the conclusion of its deliberations, the Working Group was of the view that further work on the subject of liquidated damages and penalty clauses was justified, and recommended to the Commission the holding of a further session of the Working Group. It was also of the view that the Secretariat should submit to that session a further study focusing on the following issues:

(a) The manner in which liquidated damages and penalty clauses are drafted and used in various types of international trade contracts;

(b) The particular types of international trade contracts which might usefully be regulated by uniform rules;

(c) The legal difficulties encountered in the use of liquidated damages and penalty clauses, as shown by court and arbitral decisions.<sup>3</sup>

3. The Working Group also authorized the Secretariat to submit to the next session a revised set of draft rules for regulating liquidated damages and penalty clauses, if the further work of the Secretariat disclosed the desirability of drafting such a revised set of rules.<sup>4</sup>

4. At its thirteenth session, the Commission adopted the recommendation of the Working Group, and requested the Working Group to hold a further session.<sup>5</sup>

5. The present report is submitted in pursuance to the request of the Working Group. It examines the issues noted at sub-paragraphs (a), (b) and (c) of paragraph 2 above, and contains a revised set of draft rules. While the emphasis in the earlier report of the Secretary-General on liquidated damages and penalty clauses<sup>6</sup> was on the manner in which various legal systems approached such clauses, and the obstacles to unification presented by

these differing approaches, the present report concentrates on current experience in the use of liquidated damages and penalty clauses in international trade contracts. Apart from examining contracts, arbitral awards and judicial decisions, attention has also been directed to the provisions regulating liquidated damages and penalties in laws and general conditions for delivery intended to regulate international trade, and at existing attempts at unification in regard to liquidated damages and penalties.

6. The Secretariat also solicited the views of selected experts with experience in international contract practices, and these views are reflected in the report where relevant. Furthermore, at the request of the Secretariat, a questionnaire relating to the relevant issues was circulated by the International Chamber of Commerce to its national committees, and the responses received are summarized in Addendum I to this report.

7. In the analysis that follows, the term "main obligation" will be used to describe the obligation, breach of which entails the payment of liquidated damages or a penalty, while the term "accessory obligation" is used to indicate the obligation to pay liquidated damages or a penalty; and the term "promisor" is used to indicate the party under a duty to pay liquidated damages or a penalty, while the term "promisee" is used to indicate the person entitled to claim the liquidated damages or penalty.

## Part I. The manner in which liquidated damages and penalty clauses are drafted and used in various types of international trade contracts

8. The basis for the study of this issue was the Secretariat collection of contracts.<sup>7</sup> In the examination of contracts made for the purposes of the previous report, attention was directed primarily to printed clauses found in general conditions,<sup>8</sup> and it was noted that firm conclusions could not be drawn from these clauses, as the printed text may be amended or rejected before the conclusion of a contract. Furthermore, available general conditions only dealt with a few types of contract. For

<sup>1</sup> Report of the United Nations Commission on International Trade Law on the work of its twelfth session (1979), *Official Records of the General Assembly, Thirty-fourth Session, Supplement No. 17* (A/34/17), para. 31 (Yearbook . . . 1979, part one, II, A).

<sup>2</sup> Report of the Working Group on International Contract Practices on the work of its first session: A/CN.9/177 (Yearbook . . . 1980, part two, II).

<sup>3</sup> A/CN.9/177, para. 41 (Yearbook . . . 1980, part two, II).

<sup>4</sup> A/CN.9/177, para. 42 (Yearbook . . . 1980, part two, II). A set of rules drafted by the Secretariat was submitted to the first session.

<sup>5</sup> Report of the United Nations Commission on International Trade Law on the work of its thirteenth session (1980), *Official Records of the General Assembly, Thirty-fifth Session, Supplement No. 17* (A/35/17), para. 16 (Yearbook . . . 1980, part one, II, A).

<sup>6</sup> A/CN.9/161 (Yearbook . . . 1979, part two, I, C).

<sup>7</sup> This collection at present comprises a few hundred contracts and contract clauses. The material has been supplied to the Secretariat primarily by Governments. It is not restricted, however, to contracts in which a Government or Governmental enterprise is a party. The collection includes many contracts between enterprises in developed and developing countries, and also some contracts between enterprises from the Socialist States of Eastern Europe and enterprises from Western Europe and the United States of America. Examples of the following types of contracts were examined: sales (machinery, agricultural produce, general merchandise), construction, maritime transport, licensing, loans, service and leasing, mining and mineral prospecting agreements, distributorship, joint ventures, and project financing. Sample liquidated damages and penalty clauses, where the contract from which the clause was extracted was not made available, were also examined.

<sup>8</sup> A/CN.9/161, paras. 30-40, and especially para. 34 (Yearbook . . . 1979, part two, I, C).

the purposes of the present study, only clauses in concluded contracts have been examined. However, the present study did not reveal any reason to doubt the tentative conclusions reached in the earlier study.

9. In view of the work already done by the Working Group, the contracts and clauses were examined primarily for the following purposes: to determine whether international contract practices in regard to liquidated damages and penalty clauses indicated possible solutions to the difficulties experienced by the Working Group at its first session, and to determine whether such practices presented features which needed to be taken into account when formulating uniform rules. It is therefore convenient to present the findings in their relation to the main issues as embodied in the draft Rules considered at the first session of the Working Group. As requested by some members of the Working Group, examples of clauses from contracts are given where appropriate, illustrating the formulations and devices used by traders.

#### A. POSSIBLE SCOPE OF RULES APPLICABLE TO SUCH AGREEMENTS

##### 10. *Draft Rule 1*

"These Rules apply where the parties to a contract have agreed (in writing) that, in the event of failure by the promisor (debtor) to perform his obligation, or a specified obligation, under the contract, he will pay to the promisee (creditor) or forfeit to him a sum of money (or perform a specified act) (, whether by way of compensation or penalty or both)."

11. The Working Group decided that the Rules should apply to agreements in international trade contracts, irrespective of whether such agreements envisaged the payment of a sum of money by way of compensation for loss suffered, or by way of penalty in order to coerce the debtor to perform.<sup>9</sup> The present study confirmed the soundness of this decision. In many cases, the sum of money to be paid on breach was not described in the contract as either penal or compensatory, and determining whether the sum fell into one or other category would often be difficult, and sometimes impossible when parties intended the sum to be both penal and compensatory. Indeed parties do not always clearly distinguish the two concepts.

##### *Illustration:*

##### *"Penalty for delay"*

"With the exception of force majeure causes involving extension of period as set forth under . . . .

<sup>9</sup> A/CN.9/177, paras. 14-19 (Yearbook . . . 1980, part two, II). The issue as to what types of international trade contracts the Rules might cover (A/CN.9/177, para. 15) is considered in Part II below.

<sup>10</sup> A/CN.9/177, para. 15 (Yearbook . . . 1980, part two, II).

below, if there should be any delay in FOB delivery of . . . . ., a compensation of delay will be withheld from the supplier's 10% balance, . . . . ."

(Emphasis added.) (Contract for sale of pneumatic plants by West European enterprise to Asian enterprise.)

12. The wish of the parties at the time of the conclusion of the contract is to ensure that payment of the agreed sum, however it is classified, is enforceable.

##### *Illustration:*

"In the event the said liquidated damages are held by a Court of competent jurisdiction to be unenforceable for any reason whatsoever, it is hereby agreed and expressly declared that the aforesaid amounts shall be penalties." (Contract for sale of equipment by North American enterprise to foreign enterprise.)

13. The Working Group also decided that the Rules should only regulate cases where parties had agreed that, in the event of failure by the promisor to perform the main obligation, the accessory obligation should entail payment or forfeiture to the promisee of money, and should not regulate cases where the accessory obligation entailed something other than the payment or forfeiture of money.<sup>11</sup> This restriction on scope appears to be justified, as the only clauses revealed by the study were for the payment or forfeiture of money.

14. The Working Group was agreed that the Rules should be applicable, not only to cases of a promise to pay, or forfeiture of, a sum of money on total failure by the promisor to perform his obligations, but also to cases where the breach consisted of defective or partial performance.<sup>12</sup> This decision is supported by the fact that in many cases it was difficult to determine whether the breach in respect of which the liquidated damages or penalty is payable is to be construed as a case of total or partial failure of performance.

#### *Contract usage relevant to the formulation of the Rules*

##### 15. *When the promisor's duty to pay arises*

Examples were found where the duty to pay the agreed sum was activated, not by the promisor's breach of contract, but by the act of a third party to the contract:

##### *Illustration:*

"In the event that:

"(a)-(f) . . . . .

"(g) The third party or any Agency acting as an instrument thereof ceases at any time to be the

<sup>11</sup> A/CN.9/177, para. 17 (Yearbook . . . 1980, part two, II).

<sup>12</sup> A/CN.9/177, para. 19 (Yearbook . . . 1980, part two, II).

proprietor of or to control the share capital of the Borrower or Guarantor;

"(h) . . . .

"In this event the Agent may, by notifying the Borrower,

"(1) Where the credits have been advanced, declare as immediately due and payable the principal and the interest on the Loan and the Promissory Notes, as a result of which they shall immediately become due and payable." (Contract of loan by consortium of foreign banks to Latin American firm.)<sup>13</sup>

#### 16. *The agreed sum*

In most cases parties agreed not on the sum payable but on a formula for determining the sum payable depending on the circumstances of the breach. The value of the clause will depend on the extent to which it involves potentially disputable facts.

#### 17. *Mechanism for payment of agreed sum*

The Rule as presently drafted contemplates a direct payment by the promisor to the promisee,<sup>14</sup> or a forfeiture of a sum of money to the promisee. In many cases, however, the mechanism adopted for payment was to give the promisee the right to call for payment from a financial institution which had issued a bond in favour of the promisee.<sup>15</sup> Furthermore, forfeiture was found to include not merely cases of the appropriation of money already paid by the promisor to the promisee,<sup>16</sup> but also the loss of the right to unpaid money due from the promisee to the promisor.

#### *Illustration:*

"If there should be a delay in delivery of machines, equipment, installations and materials involved in the Plant as committed by Firm, a sum of . . . . will be withheld from Firm's claims or Performance Bond for each calendar day delayed." (Contract for sale of chemical plant by West European enterprise to Asian enterprise.)

18. Examples were found when the forfeiture was of sums due under other contracts between the same parties.

#### *Illustration:*

"The penalties or charges which may be provided shall apply, successively and up to the limit specified in the preceding paragraph, to invoices arising out of the contract which may be in the process of collection or transaction; to those arising out of another contract which may have the same status, in all cases within the scope of the ENTERPRISE; to any other credit which the SELLER may have in the remaining constituent parts of the ENTERPRISE; and, lastly, to the relevant guarantee." (Emphasis added.) (Contract for sale of machinery by West European enterprise to Latin American enterprise.)

#### 19. *Defining what constitutes liquidated damages and penalty clauses*

In the earlier report, attention was directed to certain clauses which, although differing in form from liquidated damages and penalty clauses, nevertheless approximated to them by serving the same purposes.<sup>17</sup> In the present survey, examples were found of clauses providing for acceleration of payments<sup>18</sup> (see illustration to paragraph 15 above), and forfeiture clauses<sup>19</sup> (see illustration to paragraph 17 above). The function that liquidated damages and penalty clauses serve as limitation clauses<sup>20</sup> was clearly brought out by several contracts which established a graduated scale of payments for delay in performance not exceeding a maximum amount.<sup>21</sup> Examples were also found of clauses where sums described as liquidated damages were payable although the acts of the promisor upon which the sums were payable did not constitute a breach.

#### *Illustration:*

"It is further agreed that this arrangement and all rights and obligations hereunder may be terminated by (Seller) at any time for any reason which it, in its sole discretion, deems desirable, provided, however, that, except in the case of default in performance by Distributor, Seller gives at least 30 days notice of its intention to do so to Distributor. Commission earned during the notice period, if and when notice is required, shall be liquidated damages resulting from said termination." (Contract between North American enterprise and foreign enterprise.)

A clause of this type may perhaps be regarded as the price payable for the exercise of an option. (See also paragraph 65 below.)<sup>22</sup>

<sup>13</sup> Such a clause derives from the traditional conception of a liquidated damages clause as constituting an accessory obligation. See also A/CN.9/161, para. 10 (Yearbook . . . 1979, part two, I, C), and paragraph 19 below.

<sup>14</sup> See also the following: "A penalty clause shall mean any clause according to which the debtor, if he fails to perform his obligation, shall be required, by way of penalty or compensation, to pay a sum of money or perform some other act." (Emphasis added.) (Article 1 of the common provisions annexed to the Benelux Convention relating to the Penal Clause, done at The Hague on 26 November 1973.)

<sup>15</sup> Formally, the payor will be the financial institution, although it will recover the money from the promisor.

<sup>16</sup> As forfeiture was envisaged in A/CN.9/161, para. 11 (Yearbook . . . 1979, part two, I, C).

<sup>17</sup> A/CN.9/161, paras. 7-12 (Yearbook . . . 1979, part two, I, C).

<sup>18</sup> A/CN.9/161, para. 10 (Yearbook . . . 1979, part two, I, C).

<sup>19</sup> A/CN.9/161, para. 11 (Yearbook . . . 1979, part two, I, C).

<sup>20</sup> A/CN.9/161, para. 12 (Yearbook . . . 1979, part two, I, C).

<sup>21</sup> See also the following: "However, the total amount of the penalty for delay in delivery may not exceed 8 per cent of the value of the goods in relation to which the delay took place." (Article 83 (3) of the CMEA General Conditions of Delivery, 1968-1975.)

<sup>22</sup> Such a clause deviates from the traditional conception of a liquidated damages clause as constituting an accessory obligation (see paras. 21 and 22 below).

### Conclusion

20. For the purpose of formulating a rule on this issue, some decisions would have to be taken on the desired scope of the Rules, and in particular as to the types of clauses to be regulated.

#### B. THE ACCESSORY NATURE OF SUCH AGREEMENTS

##### 21. Draft rule 2

"Unless the parties have agreed otherwise, the promisee is not entitled to enforce the agreement if the promisor is not liable for his failure to perform the obligation (is not in breach of his obligation) to which the agreement relates."<sup>23</sup>

22. The Working Group was generally agreed on the substance of this rule, which accords with the rules of most national legal systems. However, no contract clauses were found laying down such a rule in general terms. The normal approach adopted was to link the liability to pay the liquidated damages or a penalty to the excuses for non-performance of the main obligation specified in the contract. These specified excuses were normally circumstances defined as constituting *force majeure*, but circumstances constituting *casus fortuitus*, and acts imputable to the promisee leading to the promisor's inability to perform the main obligation were sometimes included.

##### Illustration:

"Neither . . . . . nor . . . . . shall be liable to any of the penalties mentioned in clause 14.1 or for any delay in the performance of their obligations under the present contract if such delay was due to causes attributable to 'THE ENTERPRISE' or to *force majeure* or *casus fortuitus* as indicated in clause 18." (Contract for the supply of electrical machinery by a foreign consortium to a Latin American enterprise.)

23. The effect of the operation of an excuse for non-performance of the main obligation was sometimes the cessation of the obligation to pay the liquidated damages or penalty, but was often a modification of the latter obligation to parallel a modification of the former:

##### Illustration:

"In the event of the occurrence of circumstances in the nature of *force majeure* which make it impossible for the Seller's contractual obligations to be performed, the Seller shall be entitled to extend the delivery period for a reasonable length of time or to cancel the contract, without in any case making himself liable to any kind of indemnification." (Contract

for the supply of electrical spare parts by East European firm to a Latin American firm.)

24. All contracts examined contemplated that the accessory obligation would become immediately enforceable on breach of the main obligation without the need for any further formalities by the promisee, and a few contracts expressly provided for this:

##### Illustration:

"Automatic penalties: The penalty indicated in clause 14.1 shall be applied automatically and without it being necessary to give advance notification in writing, and the delay shall be considered as having been incurred by the mere lapsing of the time limit, without any judicial or extra-judicial appeal being necessary." (Contract between a Latin American enterprise and a foreign consortium for the supply by the latter of electrical equipment.)<sup>24</sup>

25. When examining contracts in relation to this issue, it was observed that a penalty clause needed to be evaluated in the context of the whole contract. For example, while one party may negotiate the insertion of a heavy penal sum in the contract, the other may negotiate the insertion of such wide excusing circumstances in regard to performance of the main obligation that the penalty would rarely fall due.

##### 26. Exceptional cases

A few cases were found where agreed sums were payable by the promisor despite the fact that there was no breach of contract on his part. (See paragraphs 15 and 19 above.)

### Conclusions

27. Most of the contracts examined reflect the principle contained in the rule under consideration. Decisions to be taken as to the types of clauses to be regulated by the Rules (see paragraph 20 above) will determine how the exceptional cases are to be treated.

#### C. THE RELATIONSHIP BETWEEN THE RIGHT TO OBTAIN PERFORMANCE OF A CONTRACTUAL OBLIGATION AND PERFORMANCE OF AGREEMENTS ACCESSORY TO IT

##### 28. Draft Rule 3

"(1) Unless the parties have agreed otherwise, the promisee is not entitled to enforce the agreement if he requests performance of the obligation to which the agreement relates.

<sup>24</sup> See, however, the following: "A creditor who demands the enforcement of the penalty clause must make a request or a statement beforehand in cases where such a request or statement would be required in order to obtain the damages and interest due under the law." (Article 3 of the common provisions annexed to the Benelux Convention relating to the Penal Clause, done at The Hague on 26 November 1973.)

<sup>23</sup> A/CN.9/177, paras. 20-21 (Yearbook . . . 1980, part two, II).

"(2) The provision of paragraph (1) of this Rule does not apply if the agreement relates to delay in performance."

*Variant to draft Rule 3<sup>25</sup>*

"Payment of an agreed sum does not exempt the promisor from performance of the obligation, for breach of which he has paid the agreed sum, unless the parties had agreed otherwise."

**29. Differences of view within the Working Group**

Different opinions, as reflected in paragraph (1) of draft Rule 3 above, and the variant to it, were expressed on the extent to which the promisee should be entitled to claim performance both of the main obligation and the accessory obligation. Under one view, cumulative enforcement of both obligations would be harsh to the promisor, and result in unjust enrichment of the promisee. On another view, performance of the main obligation was of paramount importance to the promisee, and only enforcement of performance of the main obligation together with the payment of compensation for loss caused by defective performance, could adequately protect him. However, it is submitted that this sharp conflict may not present such serious difficulties as may appear at first sight if attention is directed to the function of the agreed sum in the particular clause. As shown below, either one of the different solutions noted above could be appropriate depending on the circumstances in question.

**30. Agreed sums payable for delay**

There was general agreement, however, that in the case of agreed sums payable for delay in performance, payment of the agreed sum did not release the promisor from performance of the main obligation. Although no contract examined was at variance with this principle, an explicit recognition of the principle (as in the illustration below) was rarely found.

*Illustration:*

"If the Contractor fails to complete the project in accordance with the Specifications and Drawings and within the time fixed by the Project Implementation Schedule or any extension of such time as provided under clause . . . the Contractor shall pay the [buyer] . . . per day from the stipulated Date of Completion until such date when the project is completed satisfactorily subject to a maximum of 10% of the total contract price stated in clause 4." (Emphasis added.) (Contract for supply of equipment by foreign enterprise to South East Asian enterprise.)

31. In such cases, cumulation of both the right to the agreed sum and to performance results logically from the fact that the agreed sum is only intended to compensate

the promisee for the loss he suffers during the period between the start of delay and ultimate performance.<sup>26</sup>

32. The agreed sum, which normally varied with the extent of delay, was subject to a maximum, and when delay continued to a point after which performance was not required by the promisee, other remedies were often provided.

*Illustration:*

"However, penalty period will not exceed half of the total delivery period stipulated under article 4 above, and if exceeded, then the (buyer) will be free to cancel the contract, but it can extend the penalty period for a further two months, if it so desires. In case of (seller's) failure to fulfil its obligation within this period too, contract will be cancelled and Performance Bond confiscated by (buyer)." (Contract for supply of pneumatic plants by West European enterprise to Asian enterprise.)<sup>27</sup>

**33. Agreed sums payable for defects in performance**

While agreed sums payable for delay were found frequently, agreed sums payable for defects in performance were rarely found.<sup>28</sup> The extent to which sums payable for defects could be claimed together with proper performance appeared to depend on the function intended to be served by the sum.

(i) *Price reduction*

34. Where the sum payable was intended as a price reduction, so as to cause an equivalence between the new price to be paid and the imperfect performance, proper performance could not additionally be claimed.

*Illustration:*

"If, in accordance with the terms of article 11.12, it proves impossible in the course of repeated tests to achieve the guaranteed values, the Buyer shall be entitled to claim *only* a reduction in the price of the machine in question equal to 1 per cent for every full percentage point of failure of the guaranteed value over the limits of the agreed or customary tolerance, provided that the total rebate shall not exceed 5 per cent of the price of the machine in question." (Emphasis added.) (Contract for sale of electrical machinery by East European enterprise to Latin American enterprise.)<sup>29</sup>

<sup>26</sup> See paragraph 67 below.

<sup>27</sup> For the right to recover a penalty stipulated for delay when the delay continues indefinitely, see paragraph 63 below.

<sup>28</sup> A/CN.9/161, para. 37 (Yearbook . . . 1979, part two, I, C).

<sup>29</sup> It would also be reasonable to provide for a penalty covering losses incurred during the period between the time a claim in respect of defects is made and the time when agreement on a price reduction is reached, where the scope of the price reduction is limited to producing an equivalence between the price to be paid and the defective performance. An example is provided in article 75, paras. 4 and 5 of the CMEA General Conditions of Delivery 1968-1975:

"4. In the cases included in paragraph 3 of this article, the buyer shall be entitled, provided that the merchandise cannot be used in the

<sup>25</sup> The Working Group decided to delete draft Rule 4. A/CN.9/177, para. 28 (Yearbook . . . 1980, part two, II).

(ii) *Cure of defect*

35. A contract might provide that the party receiving defective performance is entitled to require the other party to cure the defective performance. In such a case, if an agreed sum is provided to cover losses occurring in the period elapsing between the time the cure is requested and the cure is effected, payment of the agreed sum would not release the promisor from making proper performance by effecting the cure.

*Illustration:*

"In the event Seller does not make warranty replacement or repairs within 5 (five) working days from receipt of notice, Seller shall pay a penalty of 1 (one) per cent per week or any part of a week commencing after expiration of said 5 days . . . .

"In case when warranty defect is not or cannot be repaired by Seller within 35 days after receipt of notification for whatsoever reason, Buyer has the right to claim replacement of machine or to cancel the contract as to the machine concerned." (Contract for the sale by North American enterprise of agricultural machinery to East European enterprise.)<sup>30</sup>

36. *Claim to agreed sums as sole remedy*

Sometimes contracts which stipulated that an agreed sum was payable on a failure of performance did not contemplate both the recovery of the agreed sum and enforcement of performance:

*Illustrations:*

(a) "Should the buyer refuse to take delivery of the goods or to effect payment, we shall be entitled to withdraw from the contract and to claim at our option either total compensation, or without any kind of official attestation the refund of 10% of the goods' value on account of lost profit." (Contract for sale of goods by East European enterprise to foreign enterprise.)

due manner, to claim from the seller payment of a penalty for delay in delivery, in the amount which is laid down in article 83, from the date of presentation of the claim to the day on which the defect was eliminated or other merchandise delivered in substitution for the defective merchandise. However, the total amount of the penalty with respect to a batch or a unit of the merchandise, including the penalty for delay in delivery, should there have been such a delay and should the amount of this penalty already have been charged, may not exceed 8 per cent of the value of the defective merchandise or the defective part of the merchandise, subject to rectification or substitution.

"5. In cases where the parties agree on a reduction in the price of the merchandise instead of a correction of the defect, in deciding on the amount of the rebate they shall agree on whether the penalty calculated or charged in accordance with paragraph 4 of this article shall be included in the amount of the rebate or added to it."

For another such provision, see article 31, paras. 5 and 6.

<sup>30</sup> See also article 75, paras. 4 and 5 of the CMEA General Conditions of Delivery, 1968-1975, quoted in the preceding footnote.

In the above case, if the buyer refuses to take delivery and the seller elects to claim 10% of the goods' value, it is apparent that he cannot also claim the price.<sup>31</sup>

(b) "In the event of any breach by the Conference of Clause 3 hereof (resulting in the shipper being unable to ship a parcel of Conference cargo within a reasonable time or at all) the Conference will pay to the shipper damages suffered thereby or a sum equal to 80 per cent of the freight (excluding trans-shipment additional) payable to one or more Members of the Conference in respect of such parcel or which would have been payable to them if such parcel had been shipped in one or more of their vessels whichever is the less and the shipper shall have the right immediately to cancel the agreement." (Agreement between a liner conference and a shipper.)

37. *Existing rules*

The existing uniform rules, and laws intended to regulate international trade contracts, appear *at first sight* to adopt different principles on the issue under consideration, matching the differences of view reflected in draft Rule 3 and the variant to it (see paras. 28-29 above). The following appear to give the promisee the right to enforce cumulatively the main and the accessory obligations:

(a) "The payment of the conventional fine does not exonerate the debtor from performance of the obligation secured by the fine." (Section 192, Czechoslovak International Trade Code.)

(b) "A penalty can be claimed in addition to the performance of an obligation." (Section 304 (1), International Commercial Contracts Act of the German Democratic Republic.)<sup>32</sup>

<sup>31</sup> For a provision of the same nature, see CMEA General Conditions of Delivery, 1968-1975, article 86:

"1. In the event of failure to meet the delivery date in fixed-term contracts, the seller shall pay the buyer a penalty in the amount of 5 per cent of the value of the merchandise which was not supplied, unless another sum is fixed for the penalty in a bilateral agreement or in the contract.

"2. If not otherwise stipulated in a bilateral agreement or in the contract, in the event of failure to meet the delivery date in fixed-term contracts the buyer shall be entitled, on cancellation of the contract, to claim from the seller compensation for damage due to failure of performance instead of the penalty provided for in paragraph 1 of this article.

"3. If in a fixed-term contract the buyer consents to receive the merchandise with a delay, the penalty provided for in paragraph 1 of this article shall not be imposed. In this case the seller shall pay the buyer a penalty for every day of delay starting from the first day of delay, in the amount specified in article 83."

If the buyer elects to obtain the 5% penalty under paragraph 1, he cannot concurrently claim performance. If he elects to receive performance despite the delay (paragraph 3), he is only entitled to a penalty at a different rate.

<sup>32</sup> The Commentary to the Act notes that parties may agree that only performance, or only the penalty, is recoverable. (*Kommentar zum Gesetz über internationale Wirtschaftsverträge—GIW—vom 5. Februar 1976, Berlin, 1978, p. 424.*)



38. A different stand appears to be adopted in the following:

(c) "The creditor may not lay claim to cumulative enforcement of the penalty clause and of the obligation to which it applies." (Article 2 (1) of the common provisions annexed to the Benelux Convention relating to the penal clause.)

(d) "The promisee may not obtain concurrently performance of the principal obligation, as specified in the contract, and payment of the sum stipulated in the penal clause unless that sum was stipulated for delayed performance. Any stipulation to the contrary shall be void." (Article 2 of the appendix to Resolution (78) 3 adopted by the Committee of Ministers of the Council of Europe.)

### 39. Possible reconciliation

Contract practice clearly suggests that a possible approach to reconciling these apparently different positions may be found on the basis of the function contemplated by the parties as being served by the agreed sum i.e. either as a substitute for performance (no cumulative enforcement of penalty and performance), or as stimulation of proper performance and compensation for loss occurring between the time proper performance is due and it is actually rendered (cumulative enforcement permissible).

## D. THE RELATIONSHIP BETWEEN THE RIGHT TO OBTAIN PERFORMANCE OF THE ACCESSORY OBLIGATION AND DAMAGES FOR BREACH OF THE CONTRACTUAL OBLIGATION TO WHICH IT IS ACCESSORY

### 40. Draft Rule 5

#### Variant A

"(1) Unless the parties have agreed otherwise, the promisee is not entitled to claim damages but can only enforce the agreement.

"(2) Nevertheless, the promisee is not entitled to a sum of money in excess of the sum stipulated in the agreement or in excess of the amount of damages which he could have claimed if no such sum had been stipulated, whichever is the larger."

#### Variant B

"(1) In case of non-performance of the principal obligation the promisee is entitled to obtain the sum of money or to request the performance of the act as stipulated in the penalty clause. The parties may agree that such sum of money or such act constitute a minimum and that the promisee may claim full compensation. In such a case the promisee must prove his actual loss before the competent court.

"(2) The parties may agree that the sum of money stipulated by the agreement constitutes a maximum amount and that the promisor may obtain a reduction of the sum stipulated to an amount of damages actually suffered by the promisee. In such a case the promisor must prove his claim before the competent court."

#### Variant C

"Unless the parties have agreed otherwise, the promisee, in addition to the sum stipulated, can obtain damages in respect of the failure to perform the contractual obligation to the extent that damages exceed the amount of the sum stipulated."

41. Divergent views were expressed on this issue in the Working Group, and these are reflected in the above variants.<sup>33</sup>

### 42. Exclusive recovery of agreed sum

Many examples were found of this principle (variant A (1)), particularly in regard to agreed sums payable for delay in performance.

#### Illustration:

"The payment of liquidated damages of up to 10 per cent of the Contract value will represent the limit of the Contractor's liability" (for delay in supplying equipment). (Contract for supply of equipment by foreign firm to South-East Asian firm.)<sup>34</sup>

### 43. Recovery of agreed sum and recovery of damages as alternative remedies

Examples of this principle were not frequent. Some illustrations are given at paragraph 36 above.

### 44. Recovery of agreed sum and damages to the extent loss exceeds such sum

A few examples of this principle (variant B, paragraph (1) and variant C) were found:

#### Illustration:

"In case of a delay in delivery a penalty of ½ % per day will be established, which does not affect, how-

<sup>33</sup> A/CN.9/177, paras. 29-36 (Yearbook . . . 1980, part two, II).

<sup>34</sup> See also: (a) Section 193 of the Czechoslovak International Trade Code: "If a conventional fine has been agreed on or otherwise provided for, the creditor shall have no right to damages for loss suffered as result of the breach of the obligation secured by the conventional fine."

(b) Chapter 13, §4, 13.4.1, of the General Conditions of Delivery of Goods from the Member Countries of the Council of Mutual Economic Assistance to the Republic of Finland and from the Republic of Finland to the Member Countries of the Council for Mutual Economic Assistance, 1980: "If the contract provides for liquidated damages in case of delay in delivery and does not provide otherwise, the buyer shall not be entitled to claim other indemnification of damages caused by the seller's delay in delivery, than the liquidated damages."

(c) Article 2 (2) of the common provisions annexed to the Benelux Convention relating to the penal clause, done at The Hague on 26 November 1973: "That which is due pursuant to the penalty clause shall be substituted for damages due under the law."



ever, Seller's liability to re-imburse the actual damages (damages arisen from the hedge buying effected by Buyers, etc.) beyond the amount of the penalty." (Contract of sale between East European enterprise and foreign enterprise.)<sup>35</sup>

45. No example was found of a contract providing that in addition to the agreed sum, damages covering the full loss suffered was recoverable. Nor was an example found of a contract providing that the promisor might prove that the extent of the actual loss was less than the agreed sum, and pay only compensation for the actual loss. (Variant B (2).)<sup>36</sup>

### Conclusions

46. Contract practice appears to support the principles contained in variant A (1) and variant B (1). It may be noted that there is no substantial difference in the principles contained in these variants.

### E. LIMITATIONS ON THE FREEDOM OF THE PARTIES TO STIPULATE A SUM OF MONEY BY WAY OF PENALTY, AND THE POWER OF COURTS AND ARBITRAL TRIBUNALS TO MODIFY THE AMOUNT OF THE SUM STIPULATED

#### 47. Draft Rule 6

##### Variant A

"An agreement stipulating a sum payable on breach of the contract shall be void if it is grossly excessive in relationship to both (a) the harm that could reasonably

<sup>35</sup> See also Section 304 (2) of the International Commercial Contracts Act of the German Democratic Republic: "Where in any contract a penalty has been agreed, it must be applied towards the damages."

The Commentary explains that, in the absence of agreement to the contrary, the promisee is free to prove that the amount of his loss exceeds the penalty, and recover such excess.

(See *Kommentar zum Gesetz über internationale Wirtschaftsverträge*—GIW—vom 5. Februar 1976, Berlin, 1978, pp. 424 et seq.)

<sup>36</sup> However, article 75 of the CMEA General Conditions of Delivery provides, *inter alia*, that, where defective goods are delivered, the buyer may ask for a reduction of the price (art. 75 (2)). The article also provides that the buyer is entitled to a penalty for the loss suffered between the date of his claim and the date of agreement to reduce the price (art. 75 (5)). The parties can agree that the amount of the price reduction includes the amount of the penalty payable. Paragraph 6 provides as follows:

"6. If the parties have agreed on the amount of the rebate but have not reached an agreement on whether the penalty provided for in paragraph 4 of this article should be included in the amount of the rebate or whether it should be added thereto, then in cases where the actual losses incurred by the buyer because of not having utilized the merchandise up to the time an agreement is reached on the rebate were less than the amount of the penalty, the penalty charged or paid shall be reduced to the amount of the actual losses; and, in the cases where the losses were greater than the penalty, the amount by which the actual losses exceed the penalty shall be paid to the buyer by the seller if so provided in a bilateral agreement." (Emphasis added.)

A similar provision is found in article 31, when a claim is made for a defect covered by a guarantee during the guarantee period, and the remedies of a price reduction together with a penalty are adopted by the parties (see art. 31 (7)).

have been anticipated from the breach, and (b) the actual harm caused thereby. The foregoing relationships are not excessive to the extent that such harm cannot be precisely predicted or established."

##### Variant B

"The sum stipulated may be reduced by the court when it is manifestly excessive, but only where such sum did not constitute a genuine pre-estimate by the parties of the damage likely to be suffered by the promisee."

##### Variant C

A provision to the effect that a court should not have the power to modify the sum stipulated.

##### Variant D

"Any penalty clause the amount of which, at the time when it was stipulated, was manifestly excessive in relation to the damages which could be foreseen as the consequence of non-fulfilment of the obligation, is deemed not to have been written."

48. Divergent views were expressed in the Working Group on this issue, and these are reflected in the above variants.<sup>37</sup> A few examples were found where the parties had indicated their wishes as regards this issue. However, their wishes would be subject to a mandatory rule of law.

##### Illustrations:

(a) "The rates of agreed and liquidated damages shall not be increased or decreased by arbitration." (Contract for export of non-agricultural products between North American enterprise and enterprise from Eastern Europe.)

(b) "The contractor is obliged to pay a penalty to buyer that cannot be reduced by any legal procedure." (Contract between East European enterprise and foreign enterprise.)

49. Provisions dealing with the reduction of penalties (see variant B) were found in some laws and uniform rules:

(a) "Where the penalty agreed is disproportionately high in relation to the loss which has occurred, the obligor is entitled to demand that it be reduced to a reasonable sum." (Section 304 (5) of the International Commercial Contracts Act of the German Democratic Republic.)<sup>38</sup>

(b) "A disproportionately high conventional fine may be reduced by a court to the amount of the damage actually caused with a view to the value and

<sup>37</sup> A/CN.9/177, paras. 37-39 (Yearbook . . . 1980, part two, II).

<sup>38</sup> The Commentary notes that the reduction need not be to the exact extent of the loss, but to a sum which might be a little higher. (*Kommentar zum Gesetz über internationale Wirtschaftsverträge*—GIW—vom 5. Februar 1976, Berlin, 1978, p. 425.)

the importance of the obligation." (Section 194 of the Czechoslovak International Trade Code.)<sup>39</sup>

(c) "The sum stipulated may be reduced by the court when it is manifestly excessive. In particular, reduction may be made when the principal obligation has been performed in part. The sum may not be reduced below the damages payable for failure to perform the obligation. Any stipulation contrary to the provisions of this article shall be void." (Article 7 of Resolution (78)3 on penal clauses in Civil Law adopted by the Committee of Ministers of the Council of Europe.)<sup>40</sup>

### Conclusions

50. Both the view that the agreed sum should not be reduced, and that the sum should be reduced if excessive, have support. Although the three provisions cited providing for reduction (paragraph 49 above) adopt different formulations, it would appear that their main object is to provide for a reduction which would make the sum mainly compensatory, although the reduced sum may to a minor extent exceed the compensatory damages which a national legal system might award.

## Part II. The particular types of international trade contracts which might usefully be regulated by uniform rules

### DEFINITION OF AN INTERNATIONAL CONTRACT

51. The Working Group was agreed that the proposed Rules should apply only to international trade contracts.<sup>41</sup> A definition appropriate in the context of the proposed Rules is needed of the criteria to be satisfied to make a trade contract qualify as international. Varying criteria (different nationalities of the parties to the contract, connection of the transaction with different legal systems, the subject matter of the contract) have been adopted for this purpose by legal systems and uniform rules. While a decision on this question may be premature at the present stage, it may be noted that the criterion adopted in the United Nations Convention on Contracts for the International Sale of Goods (the parties having their places of business in different States)<sup>42</sup> is simple, and could apply to the variety of contracts to which the proposed Rules might apply.

<sup>39</sup> See also article 67-B of the CMEA General Conditions of Delivery, 1968-75: "A penalty imposed pursuant to the present General Conditions of Delivery or by a bilateral agreement may not be reduced by arbitration." Penalties agreed to by the parties and outside the two categories mentioned may presumably be reduced.

<sup>40</sup> Article 4 of the common provisions annexed to the Benelux Convention relating to the penal clause, done at The Hague on 26 November 1973, is to the same effect.

<sup>41</sup> A/CN.9/177, para. 15 (Yearbook . . . 1980, part two, II).

<sup>42</sup> Article 1 of the United Nations Convention on Contracts for the International Sale of Goods (Yearbook . . . 1980, part three, I, B).

### TYPES OF INTERNATIONAL CONTRACTS IN WHICH LIQUIDATED DAMAGES AND PENALTY CLAUSES ARE USED

52. During the examination of contract clauses undertaken for the purposes of this study, it was noted that liquidated damages and penalty clauses were regularly used in several traditional types of international contracts (e.g. sales, transport, construction, agency and distributorship). However, such clauses were also used in contracts of more recent origin relating to economic development (e.g. international contracts for the licensing of technology,<sup>43</sup> and international contracts between parties associated for the purpose of executing a specific project<sup>44</sup>). An analysis of these clauses indicated, that their use was associated, not with the contract being of a certain type, but with the probable presence of some of the following features:

- (i) Breach of the main obligation was relatively easy to prove (e.g. failure to deliver on time, failure to meet a technical specification);
- (ii) The existence of some basis at the time of conclusion of the contract for estimating the loss likely to be caused from a breach. In regard to some types of contracts, norms appeared to have developed in the trade defining the limits of the agreed sums which parties might stipulate;<sup>45</sup>
- (iii) Proof of actual loss might be costly or difficult;
- (iv) Breach of the main obligation is not of so serious a character as to justify, at least initially, the ending of the relationship between the parties;
- (v) A need to limit the liability exposure of the party liable for breach of the main obligation;
- (vi) Circumstances which make it important to a party that he receive performance, and not damages for breach.

53. Almost any type of contract can contain an obligation in relation to which some of the above features are present, making the insertion of a liquidated damages or penalty clause appropriate. Certain types of contract almost always contain an obligation in regard to which such features are present (e.g. the obligation in a construction contract to complete by a specified date.) In

<sup>43</sup> *Guidelines for the acquisition of foreign technology in developing countries* (UNIDO publication, ID/98), p. 23, and *Guide for use in drawing up contracts relating to the international transfer of know-how in the engineering industry* (ECE publication TRADE/222/Rev.1), para. 75.

<sup>44</sup> *Guide for drawing up international contracts between parties associated for the purpose of executing a specific project* (ECE publication ECE/TRADE 131), para. 30.

<sup>45</sup> Thus in relation to international construction contracts it has been stated, "The rate of deduction for late performance varies with the size, complexity and importance of the project. As a general guide, the rate is frequently between .0001-.001 per cent of the contract price per day. An upper limit is not generally specified, but if one is desired 5-10% would be reasonable." *Guidelines for contracting for industrial projects in developing countries* (UNIDO publication ID/149 and Corr.1), p. 22.

other types of contract, such obligations may be less frequent. Thus, in the research contract, where one party engages the other to conduct research with a view to obtaining certain results, the duties of the research worker are often defined in a flexible manner. The objective of the research might change as the research progresses. The party commissioning the research relies for proper performance on the integrity and professional status of the research worker.<sup>46</sup> In view of these circumstances liquidated damages and penalty clauses are less often found in such contracts.<sup>47</sup>

54. The considerations set forth above suggest that it might be inadvisable to exclude any types of contract from the application of the proposed Rules. Such an attempt would also be inadvisable because of the varieties of contractual obligations, and the difficulty of fitting certain combinations of obligations into named types. However, it is possible to envisage cases where, for different reasons, application of the proposed Rules might be inappropriate.

#### GROUND OF PUBLIC POLICY

55. Many legal systems in certain areas (employment contracts, leasing contracts, loans) contain special provisions based on public policy which may relate to liquidated damages and penalty clauses.<sup>48</sup> In some instances these provisions may not apply to international contracts either because they have a purely domestic ambit, or because the abuses they seek to restrain do not usually occur in international transactions. However, States may prefer such provisions to prevail over the proposed Rules where the former are applicable to international contracts.

#### EXISTING CODIFICATIONS

56. The legal rules regulating certain areas of international trade may be codified in the form of treaties or laws at a global or regional level. Where these codifications also regulate the use of liquidated damages or penalty clauses, the view may be taken that it is preferable for these rules to prevail over the proposed Rules. Where the codification takes the form of model contracts which are in general use, much will depend on the particular contracts. If, for instance, the contracts are clearly

drafted, respond to the needs of the particular trade, and through regular use have created settled expectations among parties, it may be more convenient not to apply the proposed Rules.

#### AREAS OF LAW WITH A DISTINCTIVE CHARACTER

57. Instances may be found where, in a certain area of international trade, a liquidated damages or penalty clause is used with a special meaning or function. This will be due to special considerations relevant to that area. It may be difficult to accommodate the special features of such use in uniform Rules suited to a wide range of contracts.<sup>49</sup>

58. Whether there is a need to incorporate in the Rules a limitation as to the types of contracts to be regulated by the Rules might depend on the circumstances in which the Rules are to become applicable. Thus if the Rules were to be applicable upon a choice by the parties, it could be left to the parties not to apply the Rules to contracts to which they were unsuited.

#### Part III. The legal difficulties encountered in the use of liquidated damages and penalty clauses, as shown by court and arbitral decisions

59. The Secretariat encountered difficulties in obtaining a representative sampling of court and arbitral decisions on liquidated damages and penalty clauses in international contracts. Arbitral awards are generally regarded as confidential, and are not reported. In regard to court decisions, there was difficulty of access to decisions of many countries. Furthermore, even in jurisdictions where indexes of decisions on liquidated damages and penalty clauses were available, these indexes did not single out the decisions on clauses contained in inter-

<sup>46</sup> The rules of some professional bodies prevent the members of these bodies from inserting guarantees for performance in contracts entered into by them. "A member will decline to give a bond for the faithful performance of engineering services, unless required by foreign practice." Rule 21 of the Standards of Professional Conduct, American Institute of Consulting Engineers, set forth in *Manual on the use of consultants in developing countries* (UNIDO publication ID/3/Rev.1), annex 4. However, penalties are sometimes inserted. *Draft guide for drawing up international contracts on consulting engineering, including related aspects of technical assistance* (ECE document TRADE/GE.1/R.22/Rev.1, paras. 75-77).

<sup>47</sup> Endre Lontai, *The Research Contracts* (Leyden, A. W. Sijthoff, 1977), p. 164.

<sup>48</sup> See also A/CN.9/161, para. 14 (Yearbook . . . 1979, part two, I, C).

<sup>49</sup> See, for instance, the following comments on a penalty clause frequently used in charter-parties: "Penalty for non-performance of this agreement, proved damages, not exceeding estimated amount of freight"—"416 . . . Since the clause has been generally considered as being inoperative, and without effect on claims for damages under the charter-party, it is difficult to see the rationale for its present occurrence in English and American charter-parties. 417. Outside English and American law, the penalty clause seems, in principle, to be enforceable, but the construction of the clause, whether in its earlier or its modernized version, gives rise to various questions. For instance, does the clause apply solely to a total non-performance of the contract, such as the owners' failure to provide a vessel or the charterers' non-delivery of the cargo, or does it have effect also in the case of partial breach of the contract (a faulty performance)? Does the clause apply to the non-performance of either party, or only to non-performance by the charterer, as seems to be indicated by the use of 'estimated amount of freight' as a measure of the penalty? Does the clause apply literally as a limit of liability irrespective of the size of the damages actually sustained? 418. These and other questions do not seem to have received any clear answer in the different law systems, and it is evident that the penalty clause, due to the uncertainty in respect of its construction, may cause difficulties" *Charterparties* (Report by the UNCTAD secretariat, TD/B/C.4/ISL/13), paras. 416-418. See also part III, para. 66, below, where a penalty clause in a charter-party was given a distinctive interpretation in relation to *force majeure*.

national contracts. It is possible that a more prolonged search would reveal further relevant decisions.<sup>50</sup>

#### PROBLEMS ARISING FROM THE CONTRACT'S INTERNATIONAL CHARACTER

60. As was to be expected, decisions were found where courts had to consider the effect of foreign law on a liquidated damages or penalty clause.<sup>51</sup> The extent of the difficulty of determining which was the applicable law, and ascertaining the contents of the law, would depend on the circumstances of the case.

61. Cases also were found where courts had applied the provisions of their own law permitting them to reduce penalties, on the basis that it would be contrary to public policy to enforce the penalty in its agreed amount.<sup>52</sup>

62. In regard to the enforcement of a foreign judgement, it was decided that the misapplication of English law by a foreign court, resulting in the enforcement of a penalty instead of its invalidation, did not prevent the judgement from being enforced in an English court.<sup>53</sup>

#### INTERPRETATION OF CONTRACT

63. In several decisions, the issue involved was the interpretation of the contract in question. The majority of

such cases did not present any features of interest to the present study. The following decisions may, however, be noted:

(1) It has been observed that liquidated damages and penalty clauses are very frequently inserted in respect of delay in performance.<sup>54</sup> However, when the breach consists not in delay but non-performance, the penalty is nonetheless recoverable, as non-performance could be interpreted as indefinite delay.<sup>55</sup>

(2) Where the contractual provisions relating to remedies for breach in a contract in writing did not include a penalty clause, but it was usual in the trade in question to award compensation for loss caused by a certain type of breach by awarding a penalty at a specified rate, compensation should take the form of a penalty at that rate.<sup>56</sup>

(3) To qualify as a penalty clause, it must provide that the agreed sum is payable on breach of contract. A clause which stipulates that a buyer who requests extension of the shipment period in a C.I.F. contract may be granted the extension by the seller, provided the buyer pays the seller a sum of money as the price of the extension, is not a penalty clause.<sup>57</sup>

#### INTERPRETATION OF THE LAW

64. Many decisions dealt with the interpretation of the law, or the application of the law to the facts. Most of these decisions dealt with issues irrelevant to the present study.<sup>58</sup> The following dealt with some of the relevant issues noted above.

#### ACCESSORY NATURE OF THE PENALTY

65. If the main obligation is not valid, the promisor is under no duty to pay under the accessory obligation.<sup>59</sup>

<sup>50</sup> See para. 33 above.

<sup>51</sup> Istvan Szasz, "Chronique de jurisprudence hongroise de droit international privé (1945-1972)", *Journal du droit international*, vol. 100, no. 2 (1973), p. 460, at 494; *Azienda cecoslovaca K contro N.E. di Mersin (Turchia)*, Causa N.23/66, Corte di arbitrato della camera di commercio di Praga, *Diritto Negli Scambi Internazionali*, vol. 6 (1967), p. 283, at 295.

<sup>52</sup> Yves Derains, "Cour d'arbitrage de la Chambre de Commerce Internationale: chronique des sentences arbitrales", *Journal du droit international*, vol. 102, no. 4 (1975), p. 916, at 929 (sentence rendue dans l'affaire No. 2139 en 1974). For a similar approach to awarding compensation, see also Case No. 25, *From the practice of the Maritime Arbitration Commission (1969-1972)* (Moscow, 1972), p. 92. In draft Rule 1 at paragraph 10 above, the issue whether the proposed Rules should only apply to clauses in writing is left open.

<sup>53</sup> *Thos. P. Gonzalez Corporation v. F. R. Waring (International Pty Ltd.)* (1978) 1 *Lloyd's Law Reports* 494. See para. 19 above on this issue.

<sup>54</sup> E.g. decisions as to whether under the common law a particular clause should be qualified as a liquidated damages clause or penalty clause: *Clydebank Engineering and Shipbuilding Co. v. Don Jose Ramos Yzquierdo Y Castenada*, (1905) *Appeal Cases* 6; *Hellenic Lines Ltd. v. Embassy of Pakistan*, 467 *Federal Reporter*, 2nd Series 1150.

<sup>55</sup> *Aus der Spruchpraxis des Schiedsgerichts bei der Kammer für Aussenhandel der Deutschen Demokratischen Republik (1969-1976)* (Kammer für Aussenhandel der Deutschen Demokratischen Republik) 1977, p. 14; F. Enderlein et H. Strohbach, "Chronique de jurisprudence de la R.D.A.", *Journal du droit international*, vol. 107, no. 3 (1980), p. 692, at 720 (*Entreprise N., Budapest, Hongrie c. VEAHB E., Berlin, R.D.A.*).

<sup>50</sup> The Secretariat referred, *inter alia*, to the following material containing awards: *Yearbook Commercial Arbitration*, vols. I (1976)-IV (1979) (Kluwer B.V., The Netherlands); *Zorzecznictwa Kolegium Arbitrów przy Izbie Handlu Zagranicznego* (Wydawnictwo Prawnicze, Warszawa, 1980); *Aus der Spruchpraxis des Schiedsgerichts bei der Kammer für Aussenhandel der Deutschen Demokratischen Republik*, 1954-1968 and 1969-1976 (Kammer für Aussenhandel der Deutschen Demokratischen Republik); *Digest of Court Decisions of the American Arbitration Association*, vol. I-vol. IV, no. 1 (March 1980); *Quarterly of the Japan Commercial Arbitration Association*, vol. I (1978)—no. 71 (Oct.-Dec. 1978); *Decisions of the Moscow Foreign Trade Arbitration Commission*, part I (1934-1951)-part VII (1971-1974); and surveys of arbitral awards in recent issues of the *Journal du droit international* (Editions Techniques S.A., Paris) and the *Revue d'Arbitrage* (Librairies Techniques, Paris). As regards case law, apart from reference to available textbooks and indexes, a search of British cases after 1945 was made in the LEXIS computer library through the courtesy of Messrs. Butterworths (Telepublishing) Ltd., London. As regards the case law of the United States in the LEXIS library, a preliminary search was made through the kind assistance of Professor E. Allan Farnsworth of the Law School of Columbia University, New York. A search was also made in the EUROLEX computer library through the courtesy of the European Law Centre Ltd., London. The Secretariat is most grateful for the help provided by these searches. A commentator has recently noted that, from the reported cases, penal clauses do not appear to be a subject of frequent litigation: Georges R. Delaume, *Transnational Contracts*, vol. I, Oceana Publications Inc. (1980), § 3.04.

<sup>51</sup> For some recent instances, see *Gutachten zum Internationalen und Ausländischen Privatrecht*, 1976 (Tübingen, J. C. B. Mohr (Paul Siebeck), 1977), p. 46, at 52 (application of Netherlands law); *ibid.*, 1978 (Frankfurt am Main, Alfred Metzner Verlag, 1980), p. 35, at 40 (application of Ontario, Canada, law); *Die deutsche Rechtsprechung auf dem Gebiete des Internationalen Privatrechts im Jahre 1976* (Tübingen, J. C. B. Mohr (Paul Siebeck), 1978), p. 398, at 400 (application of Spanish law). See also *Reichsgericht in Zivilsachen*, vol. 19 (1887), p. 33.

<sup>52</sup> OLG Hamburg, 23 December 1902, 59 *Seufferts Archiv*, p. 63; T. F. 25 February 1915, *Recueil Officiel* 41, II, 138 (Swiss decision).

<sup>53</sup> *Godard v. Gray*, (1870) *Law Reports*. VI *Queens Bench*, 139.

66. Under a standard form of charter-party, penalties were payable by the charterer to the shipowner if there was delay in loading the ship. It was held that, by uniform international practice, the contract was interpreted as making the penalties payable even if the delay in loading resulted from *force majeure*. By using the standard form, parties had impliedly agreed to this interpretation.<sup>60</sup>

THE RIGHT TO OBTAIN BOTH PERFORMANCE OF THE MAIN OBLIGATION AND PAYMENT OF THE PENALTY OR LIQUIDATED DAMAGES

67. The payment of penalties due for delay in delivery of a machine does not prevent the buyer from obtaining an order for the delivery of the machine.<sup>61</sup>

THE RIGHT TO RECOVER BOTH THE PENALTY AND DAMAGES UPON BREACH OF THE MAIN OBLIGATION

68. Some decisions were found supporting the view that both the penalty and damages together were not recoverable.<sup>62</sup> However, it has also been decided that where a seller knew that the goods he was selling were intended to form part of a machine which the buyer was selling to a third party, and delay in delivery of the goods in turn caused a delay in the delivery of the machine, the seller was liable both for penalties stipulated for delay, and for the damages payable by the buyer to the third party.<sup>63</sup>

REDUCTION OF THE AGREED AMOUNT

69. The fact that no damage was suffered by the promisee, or less damage than the value of the penalty, was not a ground for denying recovery of the penalty, or reducing it, because the agreed amount had the character of a standardized indemnity.<sup>64</sup>

<sup>60</sup> Svetozar Hanak, "Chronique de jurisprudence tchecoslovaque", *Journal du droit international*, vol. 93 (1966), p. 879, at 883. See para. 57 above.

<sup>61</sup> Award in the case of the complete plant and equipment Foreign Trade Organization COMPLEX of Hungary, against V/O Tjahpromexport, No. 109, *Collected Arbitration Cases, Part IV*, The USSR Chamber of Commerce and Industry, Law Section (Moscow). The issue was decided by reference to S. 36 of the Fundamentals of Civil Law of the USSR and of the Soviet Constituent Republics.

<sup>62</sup> Award of 6 March 1941, in the case of the claim of V/O Raznoimport against the Bulgarian Joint-Stock Company Musulla and Trading House Serdika, No. 18, *ibid.*, part 1. The issue was decided by reference to article 141, note 1, of the R.S.F.S.R. Civil Code; award of 12 March 1941 in the case of the claim of V/O Vostokintorg against the Turkish firm Sümerbank (Izmir), no. 19, *ibid.*; award of 18 February 1966 in the case of Maschinen-Export (Berlin) against V/O Machinexport, no. 152, *ibid.*, part V. The issue was decided by reference to the Protocol of 11 April 1958 between the USSR and the German Democratic Republic; Istvan Szasz, "Chronique de jurisprudence hongroise de droit international privé (1945-1972)", *Journal du droit international*, vol. 100, no. 2 (1973), p. 460, at 497. The issue was decided by reference to the provisions of the CMEA General Conditions of Delivery, 1958.

<sup>63</sup> F. Enderlein et H. Strohbach, "Chronique de jurisprudence de la R.D.A.", *Journal du droit international*, vol. 107, no. 3 (1980), p. 692, at 701 (U. GmbH, R.D.A. c. Entreprise T. Yougoslavie).

<sup>64</sup> *Aus der Spruchpraxis des Schiedsgerichts bei der Kammer für Aussenhandel der Deutschen Demokratischen Republik (1954-1968)* (Kammer für Aussenhandel der Deutschen Demokratischen Republik, 1979), p. 140 (decided with reference with CMEA General Conditions of Delivery, 1958).

70. The following factors were recognized as justifying a reduction of penalties:

(a) The amount of the penalty being excessive in relation to the value of the goods, and the measure of the fault of the promisor; or

(b) The promisee contributing equally to the breach of contract.<sup>65</sup>

(c) The excessive nature of the penalty in relation to the loss suffered; or

(d) Action by the promisee in contravention of established practice contributing to his loss.<sup>66</sup>

Part IV. Revised set of draft Rules

71. The revised draft Rules, with comments, set forth below are submitted with a view to assisting the Working Group in its deliberations. The scope of these revised draft Rules is confined to the issues raised at the first session of the Working Group. They are arranged in the same order that the preliminary draft Rules were presented to the first session of the Working Group. They may need to be expanded to cover other issues which the Working Group may wish to consider (e.g. allocation of the burden of proof, consequences of rescission or cancellation of the contract by a party).

\* \* \* \* \*

SCOPE OF APPLICATION

72. Revised draft Rule 1

"These Rules apply to a contract in which the parties have agreed [in writing] that, upon a total or partial failure of performance by a party (the debtor), another party (the creditor) is entitled to recover, or to forfeit, an agreed sum of money."

Comments:

73. An attempt has been made to reflect decisions taken by the Working Group at its first session.<sup>67</sup> Accordingly, no reference is made to the object of the agreement (penalty, compensation, limitation), or to the possibility of the performance of an act by the debtor.

74. The focus has been shifted from the duty of the debtor to pay (as in the earlier draft) to the right of the

<sup>65</sup> Istvan Szasz, "Chronique de jurisprudence hongroise de droit international privé (1945-1972)", *Journal du droit international*, vol. 100, no. 2 (1973), p. 400, at 495. Reference was made to the provisions of the Hungarian Civil Code.

<sup>66</sup> The award of 7 May 1956, in the case of the Deutscher Innen-und-Aussenhandel Chemie (Berlin) against V/O Soyuzkhimexport, No. 52, *Collected Arbitration Cases, Part II*, The USSR Chamber of Commerce and Industry, Law Section (Moscow). Reference was made to article 142 of the Civil Code of the R.S.F.S.R.

<sup>67</sup> A/CN.9/177, paras. 14-19 (Yearbook . . . 1980, part two, II).

creditor to recover, in order to cover the case where the creditor recovers under a performance bond. (See para. 17 above.)

75. The following matters need consideration:

- (1) Definition of the circumstances which would make a contract qualify as international;
- (2) Whether any types of contract are to be excluded from the scope of Rules, and if so, how this should be done; and
- (3) Whether the requirement of a written agreement is to be maintained or not.

#### REGULATION OF THE CONTRACT BY THE RULES

##### 76. *Revised draft Rule 2*

"Unless the parties have agreed otherwise, the creditor is not entitled to recovery or forfeiture of the agreed sum if the debtor is not liable for the failure of performance."

#### Comments:

77. The Working Group was in general agreement<sup>68</sup> upon the substance of this Rule. It operates when there is a defence to an action for the failure, or where the right of the creditor arising from the failure is extinguished (e.g. by expiry of the prescription period). The allocation of the burden of proof may need clarification.

##### 78. *Revised draft Rule 3*

"(1) When the agreed sum is intended by the parties to be complete compensation for the loss caused by a failure of performance, the creditor cannot enforce performance if he enforces recovery, or forfeiture, of the agreed sum.

"(2) When the agreed sum is intended by the parties to compensate the creditor for the loss caused in the period between a failure of performance and the time when proper performance is rendered, the creditor may enforce performance, and also enforce recovery, or forfeiture, of the agreed sum.

"(3) Parties may by agreement provide otherwise."

#### Comments:

79. This Rule, and draft Rule 5 below, address two connected issues: regulating the combination of possible remedies, and the prevention of unfairness.

80. The Working Group was not agreed on the proper principles to regulate this issue.<sup>69</sup> To have a rule under which in all circumstances the creditor only recovered the agreed sum would result in his under-compensation in some cases. To have a rule under which the creditor in all circumstances recovered the agreed sum, and could also

enforce performance of the obligation in breach resulted in his over-compensation in some cases. An attempt is made in sub-rules (1) and (2) above to deal with two cases occurring often in practice, and to set forth acceptable results for these cases.<sup>70</sup> Under (3) above, parties are free to change these results, and to make provision for other situations.

81. It may be noted that regulating the possible combination of remedies is only one factor in preventing unfair compensation. The amount of the sum agreed as a penalty or liquidated damages is also relevant. Thus, upon an application of sub-rule (1) above, if the sum is fixed at an amount exceeding the value of the loss caused by the breach, the creditor will be over-compensated. Variation of the specified sum under draft Rule 6 may be regarded an effective remedy to unfair compensation.

##### 82. *Revised draft Rule 5*<sup>71</sup>

"If a failure of performance in respect of which parties have agreed that a sum of money is to be recoverable, or forfeited, occurs, the creditor is only entitled to recover, or forfeit, the sum, and is not entitled to damages. Parties may agree that the creditor, if he proves that his loss exceeds the amount of such sum, may also recover the amount of the excess."

#### Comments:

83. As regards the issue regulated by this Rule the principles contained in the above draft Rule were reflected most often in the contracts examined.<sup>72</sup>

##### 84. *Revised draft Rule 6*

#### Variant 1

"The agreed sum shall neither be increased nor reduced."

#### Variant 2

"The agreed sum specified may be reduced when it is [manifestly] [grossly] excessive [in relation to the loss which has occurred], but only if such sum did not constitute a genuine pre-estimate by the parties of the loss likely to be suffered by the creditor."

#### Variant 3

"An agreement of the kind described in Rule 1 above shall be void if the agreed sum is [manifestly] [grossly] excessive in relationship to both (a) the loss that could reasonably have been anticipated from the failure of performance, and (b) the actual loss caused thereby. The agreement shall not be void if the loss could not have been precisely predicted or cannot be precisely established."

<sup>70</sup> See para. 29 above.

<sup>71</sup> The Working Group decided to delete preliminary draft Rule 4. A/CN.9/177, para. 28 (Yearbook . . . 1980, part two, II).

<sup>72</sup> For the variants considered by the Working Group, see A/CN.9/177, paras. 29-36 (Yearbook . . . 1980, part two, II).

<sup>68</sup> A/CN.9/177, paras. 20-21 (Yearbook . . . 1980, part two, II).

<sup>69</sup> A/CN.9/177, paras. 22-28 (Yearbook . . . 1980, part two, II).



*Comments:*

85. The above formulations are based on variants submitted to the Working Group.<sup>73</sup> Variant 1 provides

<sup>73</sup> A/CN.9/177, paras. 37-39 (Yearbook . . . 1980, part two, II).

that the specified sum shall not be reduced, variant 2 provides that it may be reduced in certain circumstances, and variant 3 provides that it may be void in certain circumstances. Further work must depend on a decision as to which approach is to be adopted.

2. REPORT OF THE SECRETARY-GENERAL: ANALYSIS OF EXPERT OPINIONS, AND OF REPLIES TO THE SECRETARIAT QUESTIONNAIRE ON LIQUIDATED DAMAGES AND PENALTY CLAUSES (A/CN.9/WG.2/WP.33/ADD.1)\*

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ANALYSIS OF EXPERT OPINIONS, AND OF REPLIES  
TO THE SECRETARIAT QUESTIONNAIRE

*Introduction*

1. In order to obtain views on commercial practice in regard to liquidated damages and penalty clauses, and in particular as to their experience in difficulties encountered in the negotiation, drafting and enforcement of such clauses, the Secretariat solicited the opinions of selected legal experts. The Secretariat also requested the International Chamber of Commerce (ICC) to circulate a questionnaire on the subject to its national committees.<sup>1</sup>

2. Replies to the questionnaire were received from Belgium, France, Finland, Germany, Federal Republic of, India, Israel, Italy, Japan, Norway, Republic of Korea, Sweden and Turkey. The questions contained in the questionnaire are set forth below, and under each question is set forth an analysis of the replies received to that question. A few opinions were received from legal experts, and it appeared convenient to record these opinions in the present document. The opinions are contained in footnotes under each question in the questionnaire to which the opinion expressed was relevant.

\* 9 March 1981. Incorporates A/CN.9/WG.2/WP.33/Add.1/Corr.1 (English only).

<sup>1</sup> The Secretariat is most grateful to the International Chamber of Commerce for its co-operation, and to the ICC secretariat for its assistance.

*Analysis of opinions and replies**Question 1:*

3. Are provisions inserted in international contracts for the payment of liquidated damages or penalties for total or partial non-performance of contracts

- (a) often?
- (b) occasionally?
- (c) never?

4. The majority of respondents noted that such provisions were inserted often in international contracts, while some noted that they were inserted occasionally. Some respondents observed that the likelihood of the insertion of such provisions depended on the type of contract in question, such provisions being normally inserted in contracts for the supply of goods, for failure to observe the stipulated delivery time, and in contracts for the supply and erection of plant and machinery.<sup>2</sup>

*Question 2:*

5. Have you encountered difficulties in agreeing upon the insertion of such provisions in international contracts? Please give details.

6. The majority of respondents noted that, while there was often agreement on the need for such provisions, difficulties were encountered in agreeing on their contents (especially on the amount of the sum payable,

<sup>2</sup> See also the replies to question 4 below.

and the ceiling on liability). A few respondents indicated that difficulties in reaching agreement did not arise when the agreed sum had only a compensatory function, but arose when the sum was intended to go beyond compensation and provide a sanction for non-performance. It was noted that difficulties were sometimes encountered in reaching agreement as to what remedies buyers might be entitled to in addition to claiming the agreed sum.<sup>3</sup>

*Question 3:*

7. *If the answer to question 1 is either (a) or (b), in what kinds of international contracts are such provisions inserted?*

8. It was noted that such provisions were inserted in a large variety of contracts. The following types were specially mentioned: supply of goods, manufacture and installation of plant and machinery, construction contracts, joint ventures, and supply of long-term services. As regards loans, it was noted that the penalty would consist of an enhanced rate of interest.<sup>4</sup>

*Question 4:*

9. *For what types of non-performance (e.g. delay in performance, failure to meet contract standards) are such provisions usually inserted, and what are the special advantages of such provisions for those types of non-performance?*

10. All respondents noted that such provisions are usually inserted for delay in performance.<sup>5</sup> Many respon-

<sup>3</sup> (a) One expert noted that difficulties might arise in agreeing on the following matters: the law which should govern the contract and the liquidated damages or penalty clause; the measure of liquidated damages where such damages are stipulated for delay in delivery of plant or equipment (e.g. whether it should be a proportion of the value of the total unit, or of the item delayed, or the items not operable because of the delay); and the additional remedies which the buyer should have, where liquidated damages are provided for partial non-performance (e.g. output inferior to that specified) and there is total non-performance (the unit cannot be used at all).

(b) Another expert noted that difficulties might arise in ensuring that the proposed clause was enforceable under the agreed applicable law. The following solutions had been used to overcome possible difficulties in this regard (i) contracts in the alternative (i.e. a contract that specifies differing obligations for alternative qualities, quantities or timings of performance) (ii) discounts for early payment or premiums for early performance (iii) acceleration clauses and (iv) provision of the right to cancel the contract before it would otherwise be terminated, conditioned on a cancellation payment. One of the above solutions may be more appropriate to a particular contract, or more acceptable to a particular party.

<sup>4</sup> One expert noted that the type of contract in question was one of several factors which were considered as a whole when deciding on whether to insert such provisions. Other factors were: the importance of the proposed undertaking (e.g. the timing of completion might have developmental or political implications); difficulties of proving loss in respect of particular types of breach; the likely treatment of such provisions by the applicable law; and the attitude to such clauses of the forum chosen to settle disputes.

<sup>5</sup> One expert noted that it was not always possible to agree on a quantification of the loss which might be caused by delayed performance (e.g. quantification of lost profits caused by the failure to deliver a unit on time, the loss caused by the adverse "spread" effect to other economic activities resulting from the absence of the unit). At the same time, it was noted that even where quantifiable, the costs of delay (e.g. in a large scale industrial development project) might be so great that no contractor would agree to a liquidated damages clause covering such costs.

dents also indicated that they were sometimes inserted for failure to meet specified contract standards, usually in contracts for the supply of goods, including plant and machinery.

*Question 5:*

11. *Have you encountered any difficulties in the application or enforcement of such provisions in international contracts? Please give details. In particular, have liquidated damages or penalties*

(a) *been declared void?*

(b) *been reduced by Courts or arbitral tribunals?*

12. Most respondents noted that they had not encountered any difficulties, and that in their experience liquidated damages and penalty clauses had not been declared void, nor the agreed amounts reduced. A few respondents indicated that such clauses were rarely declared void, except when the agreed amount was grossly excessive. The agreed amounts were sometimes reduced when the judge or arbitrator had the power of reduction. It was also observed that parties sometimes amicably settled out of court disputes as to payment of liquidated damages and penalties.<sup>6</sup>

*Question 6:*

13. *Would the drawing up of a uniform law applicable to international contracts and reducing the difficulties which arise in the use of such provisions be worthwhile?*

14. Respondents were evenly divided on this issue. Those who observed that the drawing up of a uniform law would be worthwhile adduced the following reasons in support of their views: a uniform law would reduce the difficulties caused by the differences in national laws on liquidated damages and penalties; such a law would reduce negotiations on issues covered by it, and in any event provide a guideline as to issues to be covered; and a uniform law would provide better remedies to the party entitled to liquidated damages or a penalty.

15. Those who observed that the drawing up of a uniform law would not be worthwhile adduced the following reasons in support of their view: States were hesitant to accept uniform laws in the field of contract, and in particular States which had national laws to check abuses of liquidated damages and penalties would be

<sup>6</sup> (a) One expert noted that a technique used to enhance the validity of such provisions was, as a first step, to try to reach agreement on the applicable law and the forum for the settlement of disputes. Thereafter, the clause would be drafted so as to maximize the likelihood of its validity being upheld under the selected law and by the selected forum. It was noted, however, that there may be difficulty in agreeing on the law and the forum, and that there may also be limits to the extent to which parties could make a choice of law or forum.

(b) Another expert noted that difficulties often arose when the original plan in a construction contract was modified, but corresponding adjustments were not made to the liquidated damages and penalty clauses. Difficulties also arose where parties provided an overall ceiling for aggregate liquidated damages, but failed to state clearly what the remedies would be if performance was totally defective.



reluctant to exclude international commercial contracts from their sphere of application; the difficulties in this area were of a practical nature and varied with each contract, and could not be resolved by a uniform law; and the text of a uniform law would be of a vague and general character, and therefore of doubtful value.

*Question 7:*

16. *Are there any approaches, other than the drafting of a uniform law, which might reduce the difficulties currently encountered by parties in the use of liquidated damages and penalty clauses (e.g. the drawing up of guidelines to assist parties wishing to use a liquidated damages or penalty clause)?*

17. Two other possible approaches were noted. Firstly, the drawing up of standard contracts or general conditions, which would contain terms resolving the difficulties currently encountered. Secondly, the drawing up of guidelines, with an analysis of the problems encountered, and possible solutions to such problems.

18. Most of the respondents opposed to the drafting of a uniform law saw some merit in one or the other of the above approaches, and a few of the respondents supporting the drafting of a uniform law saw merit in the above approaches as alternatives to a uniform law.<sup>7</sup>

<sup>7</sup> One expert noted that the drafting of standard or model clauses was not desirable because immunity of a liquidated damages or penalty clause from attack on grounds of public policy, or other grounds, depended primarily on the clause being reasonable in relation to the circumstances of the particular contract in which it was contained.

**C. Report of the Secretary-General: clauses protecting parties against the effects of currency fluctuations (A/CN.9/201)\***

1. The Commission, at its eleventh session, decided that, as part of the general study of international contract practices, consideration should be given to clauses in international trade contracts by which parties seek to protect themselves against the effects of currency fluctuations.<sup>1</sup> At that session it requested the Secretary-General to make a preparatory study of the question.

2. The Commission, at its twelfth session, had before it a report of the Secretary-General entitled "Clauses protecting parties against the effects of currency fluctuations".<sup>2</sup> The report described the commercial reasons for clauses designed to protect creditors against changes of the value of a currency in relation to other currencies and for clauses by which creditors seek to maintain the purchasing value of the monetary obligation under the contract. The report examined the various kinds of clauses designed to accomplish these two results and con-

*Question 8:*

19. *Are there any other observations you wish to make?*

20. Most respondents made no other observations. Those who replied to this question made the following observations on negotiating liquidated damages and penalty clauses:

(1) A ceiling should always be placed on the amount payable. This ceiling should generally be 5% to 8% of the amount of the contract;

(2) In lump-sum contracts, which are very frequent in the industrial construction sector, liquidated damages or penalties should only be inserted for failure to observe the final date of delivery. They should not be inserted for non-compliance with the successive stages of manufacture, transport, and erection;

(3) The contract should not contain provision for the deduction of liquidated damages or penalties from sums due to the supplier;

(4) Clauses providing liquidated damages or penalties for delay were often combined with clauses providing a bonus for early performance.

sidered the legal and policy framework in which such clauses operate in a selected number of countries.

3. The Commission, at its twelfth session, recognized that the subject was of current interest because of the floating of the major trade currencies.<sup>3</sup> There was wide agreement that the development of clauses of the type described in the report would benefit international trade. However, doubts were expressed in the Commission whether such clauses were effective as a safeguard against currency fluctuations or world-wide inflation. The view was also expressed that it was doubtful whether it was possible for the Commission to regulate on a world-wide basis the content of clauses that sought to eliminate most or all of the monetary risks involved in long-term contracts.

4. As a result, the Commission requested the Secretariat to carry out further studies in respect of clauses protecting parties against the effects of currency fluctua-

\* 2 April 1981. Referred to in Report, para. 48 (part one, A, above).

<sup>1</sup> *Official Records of the General Assembly, Thirty-third Session, Supplement No. 17 (A/33/17)*, para. 67 (Yearbook . . . 1978, part one, II, A).

<sup>2</sup> A/CN.9/164 (Yearbook . . . 1979, part two, I, D).

<sup>3</sup> *Official Records of the General Assembly, Thirty-fourth Session, Supplement No. 17 (A/34/17)*, paras. 32 to 40 (Yearbook . . . 1979, part one, II, A).

tions, and, with specific reference to the desirability and feasibility of work by the Commission on this topic, to submit a report on its findings to the Commission with appropriate recommendations.<sup>4</sup>

5. The Secretariat is currently studying the problems caused by currency fluctuations in two contexts.

(1) The Commission will have before it at the present session a report on a universal unit of account of constant value for use in international conventions.<sup>5</sup> The report suggests the use of the SDR linked to an appropriate index with adjustments made for non-member States of the International Monetary Fund. As was noted at the twelfth session, the problem is not identical to that involving international trade contracts.<sup>6</sup> However, since the decision of the International Monetary Fund to change the composition of the SDR from a 16 currency basket to a 5 currency basket, there has been a revival of interest in the use of the SDR in private financial transactions. Therefore, the conclusions reached in respect of the unit of account will be relevant to some international contracts.

(2) The Secretariat has presented to the second session of the Working Group on the New International Economic Order, which meets from 9 to 18 June 1981 at Vienna, the first half of the study in respect of contracts for the supply and construction of large industrial works.<sup>7</sup> The second half of the study, which is expected to be presented to the third session of the Working Group, will contain the studies in respect of the price, including the clause on price revision and the clause on currency and rates of exchange.<sup>8</sup>

6. It has become evident from the studies conducted so far that the monetary problems are different, and the

most appropriate solution may also be different, if the contract involves

The periodic delivery of goods over a period of time; a charter-party;<sup>9</sup>

An international loan in the Eurocurrency market,<sup>10</sup> or the construction of a large industrial plant.

7. In some types of contract it may be important to match the currencies of account, and perhaps also of payment, to the currencies in which the creditor will incur his costs. In other types of contract, it may be important to use a currency or unit of account which has no relationship to the currencies in which the creditor will incur his costs or in which the debtor will resell or otherwise recoup his expenditure. Not only do these decisions affect the nature of the clause in respect of the currency and rate of exchange, it also affects the nature of the clause in respect of maintenance of purchasing value. These issues become more complex as the international monetary system is still in the process of change.

8. That difficulty has already been experienced by the Committee on International Monetary Law of the International Law Association which was first requested by the Conference of the Association in The Hague in 1970 to propose several types of formula for currency exchange guarantees based on a unit of account. In view of the substantial work undertaken in this matter and in respect of maintenance of value clauses by the Committee, the Secretariat will remain in contact with the Committee for any new developments.

9. Therefore, the Commission may wish to request the Secretary-General to continue his studies of clauses by which parties seek to protect themselves against currency fluctuations as described in paragraph 5 above.

<sup>4</sup> *Ibid.*, para. 40.

<sup>5</sup> A/CN.9/200 (reproduced in this volume, part two, II, C).

<sup>6</sup> A/CN.9/SR.213, para. 7.

<sup>7</sup> A/CN.9/WG.V/WP.4, and Add.1 to 8 (reproduced in this volume, part two, IV, B, 1).

<sup>8</sup> A/CN.9/WG.V/WP.4 (reproduced in this volume, part two, IV, B, 1).

<sup>9</sup> See, S. Mankabady, "The currency, escalation and bunker clauses in charter-parties", *The International Contract*, vol. 6 (1980), p. 361; L. Gorton, "Escalation and currency clauses in shipping contracts", *Journal of World Trade Law*, vol. 12 (1978), p. 319.

<sup>10</sup> See, A. Jacquemont, "Le contrat d'euro-crédit: un contrat à contenu variable," *Journal du droit international*, vol. 106 (1979), p. 34.

## II. INTERNATIONAL PAYMENTS\*

### A. Report of the Working Group on International Negotiable Instruments on the work of its tenth session (Vienna, 5-16 January 1981) (A/CN.9/196)\*\*

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#### Introduction

1. In response to decisions by the United Nations Commission on International Trade Law (UNCITRAL), the Secretary-General prepared a draft Uniform Law on International Bills of Exchange and International Promissory Notes, with commentary (A/CN.9/WG.IV/WP.2).<sup>1</sup> At its fifth session (1972), the Commission established a Working Group on International Negotiable Instruments. The Commission requested that the above draft Uniform Law be submitted to the Working Group and entrusted the Working Group with the preparation of a final draft.<sup>2</sup>

2. The Working Group held its first session in Geneva in January 1973. At that session the Working Group considered articles of the draft Uniform Law relating to transfer and negotiation (articles 12 to 22), the

rights and liabilities of signatories (articles 27 to 40), and the definition and rights of a "holder" and a "protected holder" (articles 5, 6 and 23 to 26).<sup>3</sup>

3. The second session of the Working Group was held in New York in January 1974. At that session the Working Group continued consideration of articles of the draft Uniform Law relating to the rights and liabilities of signatories (articles 41 to 45) and considered articles in respect of presentment, dishonour and recourse, including the legal effects of protest and notice of dishonour (articles 46 to 62).<sup>4</sup>

4. The third session was held in Geneva in January 1975. At that session the Working Group continued its consideration of the articles concerning notice of dishonour (articles 63 to 66). The Group also considered provisions regarding the sum due to a holder and to a party secondarily liable who takes up and pays the instrument (articles 67 and 68) and provisions regarding the circumstances in which a party is discharged of his liability (articles 69 to 78).<sup>5</sup>

5. The fourth session of the Working Group was held in New York in February 1976. At that session the Working Group considered articles 79 to 86 and articles 1

\* For consideration by the Commission see Report, chapter II (part one, A, above).

\*\* 16 February 1981. Referred to in Report, paras. 12, 13, 14, 15 (part one, A, above). See also Note by the Secretariat: Alternative methods for the final adoption of conventions emanating from the work of the Commission (A/CN.9/204), reproduced in this volume, part two, VIII.

<sup>1</sup> Report of the United Nations Commission on International Trade Law on the work of its fourth session, *Official Records of the General Assembly, Twenty-sixth Session, Supplement No. 17* (A/8417), para. 35 (Yearbook . . . 1971, part one, II, A). For a brief history of the subject up to the fourth session of the Commission, see A/CN.9/53, paras. 1 to 7. See also Report of the United Nations Commission on International Trade Law on the work of its fifth session, *Official Records of the General Assembly, Twenty-seventh Session, Supplement No. 17* (A/8717), para. 61 (2) (c) (Yearbook . . . 1972, part one, II, A).

<sup>2</sup> Report of the United Nations Commission on International Trade Law on the work of its fifth session, *Official Records of the General Assembly, Twenty-seventh Session, Supplement No. 17* (A/8717), para. 61 (1) (a) (Yearbook . . . 1972, part one, II, A).

<sup>3</sup> Report of the Working Group on International Negotiable Instruments on the work of its first session (Geneva, 8-19 January 1973), A/CN.9/77 (Yearbook . . . 1973, part two, II, 1).

<sup>4</sup> Report of the Working Group on International Negotiable Instruments on the work of its second session (New York, 7-18 January 1974), A/CN.9/86 (Yearbook . . . 1974, part two, II, 1).

<sup>5</sup> Report of the Working Group on International Negotiable Instruments on the work of its third session (Geneva, 6-17 January 1975), A/CN.9/99 (Yearbook . . . 1975, part two, II, 1).

to 11 of the draft Uniform Law, thereby completing its first reading of the draft text of that law.<sup>6</sup>

6. At the fifth session of the Working Group, held in New York in July 1977, the Working Group commenced its second reading of the draft Uniform Law (retitled at that session "draft convention on international bills of exchange and international promissory notes") and considered articles 1 to 24.<sup>7</sup>

7. The sixth session of the Working Group was held in Geneva in January 1978. At that session the Working Group, continuing its second reading of the text of the draft Convention on International Bills of Exchange and International Promissory Notes, considered articles 5 and 6 and articles 24 to 53.<sup>8</sup>

8. The seventh session of the Working Group was held in New York in January 1979. At that session the Working Group, continuing its second reading of the text of the draft Convention on International Bills of Exchange and International Promissory Notes, considered articles 24 and 53 to 70.<sup>9</sup>

9. The eighth session of the Working Group was held in Geneva in September 1979. At that session the Working Group, continuing its second reading of the text of the draft Convention on International Bills of Exchange and International Promissory Notes, considered articles 1, 5, 9, 11 and 70 to 86.<sup>10</sup> In response to a decision by the Commission at its twelfth session,<sup>11</sup> the Working Group, at its eighth session, requested the Secretariat to commence preparatory work in respect of uniform rules applicable to international cheques.

10. The ninth session of the Working Group was held in New York in January 1980. At that session the Working Group, continuing its third reading of the text of the draft Convention on International Bills of Exchange and International Promissory Notes, considered articles 13 to 85 and article 5(10) in connexion with article 22.<sup>12</sup> The Working Group also considered articles 1 to 30 of the uniform rules applicable to international

cheques as drafted by the Secretariat (A/CN.9/WG.IV/ WP.15).

11. The Working Group held its tenth session at Vienna from 5 to 16 January 1981. The Working Group consisted of the following eight members of the Commission: Chile, Egypt, France, India, Nigeria, Union of Soviet Socialist Republics, United Kingdom of Great Britain and Northern Ireland and United States of America. All members of the Working Group were represented at the tenth session. The session was also attended by observers of the following States: Argentina, Australia, Austria, People's Republic of China, Cuba, German Democratic Republic, Germany, Federal Republic of Italy, Japan, Luxemburg, Malaysia, Netherlands, Pakistan, Philippines, Poland, Republic of Korea, Spain, Switzerland, Thailand, Trinidad and Tobago, and Turkey, and by observers from the International Monetary Fund, the Bank for International Settlements, the Hague Conference on Private International Law, the European Banking Federation and the International Chamber of Commerce.

12. The Working Group elected the following officers:

Chairman: ..... Mr. René Roblot (France)

Rapporteur: ..... Mr. Essam El-Din Hawas (Egypt)

13. The Working Group had before it the following documents: provisional agenda (A/CN.9/WG.IV/ WP.18); draft uniform law on international bills of exchange and international promissory notes, with commentary (A/CN.9/WG.IV/ WP.2); draft uniform law on international bills of exchange and international promissory notes (first revision) (A/CN.9/WG.IV/ WP.6 and Add. 1 and 2); note by the Secretariat: desirability of preparing uniform rules applicable to international cheques (A/CN.9/WG.IV/ CRP.5); draft convention on international bills of exchange and international promissory notes (first revision) articles 46 to 68 as reviewed by a drafting party (A/CN.9/WG.IV/ WP.10); draft convention on international bills of exchange and international promissory notes (first revision) articles 24 and 68 to 86 as reviewed by a drafting party (A/CN.9/WG.IV/ WP.12); the respective reports\* of the Working Group on the work of its first (A/CN.9/77), second (A/CN.9/86), third (A/CN.9/99), fourth (A/CN.9/117), fifth (A/CN.9/141), sixth (A/CN.9/147), seventh (A/CN.9/157), eighth (A/CN.9/178), and ninth (A/CN.9/181) sessions; draft convention on international bills of ex-

<sup>6</sup> Report of the Working Group on International Negotiable Instruments on the work of its fourth session (New York, 2-12 February 1976), A/CN.9/117 (Yearbook . . . 1976, part two, II, 1).

<sup>7</sup> Report of the Working Group on International Negotiable Instruments on the work of its fifth session (New York, 18-29 July 1977), A/CN.9/141 (Yearbook . . . 1978, part two, II, A).

<sup>8</sup> Report of the Working Group on International Negotiable Instruments on the work of its sixth session (Geneva, 3-13 January 1978), A/CN.9/147 (Yearbook . . . 1978, part two, II, B).

<sup>9</sup> Report of the Working Group on International Negotiable Instruments on the work of its seventh session (New York, 3-12 January 1979), A/CN.9/157 (Yearbook . . . 1979, part two, II, A).

<sup>10</sup> Report of the Working Group on International Negotiable Instruments on the work of its eighth session (Geneva, 3-14 September 1979), A/CN.9/178 (Yearbook . . . 1980, part two, III, A).

<sup>11</sup> Report of the United Nations Commission on International Trade Law on the work of its twelfth session, *Official Records of the General Assembly, Thirty-fourth Session, Supplement No. 17* (A/34/17), para. 44 (Yearbook . . . 1979, part one, II, A).

<sup>12</sup> Report of the Working Group on International Negotiable Instruments on the work of its ninth session (New York, 2-11 January 1980), A/CN.9/181 (Yearbook . . . 1980, part III, B).

\* Yearbook references for the reports mentioned in this paragraph are as follows: A/CN.9/77: Yearbook . . . 1973, part two, II, 1; A/CN.9/86: Yearbook . . . 1974, part two, II, 1; A/CN.9/99: Yearbook . . . 1975, part two, II, 1; A/CN.9/117: Yearbook . . . 1976, part two, II, 1; A/CN.9/141: Yearbook . . . 1978, part two, II, A; A/CN.9/147: Yearbook . . . 1978, part two, II, B; A/CN.9/157: Yearbook . . . 1979, part two, II, A; A/CN.9/178: Yearbook . . . 1980, part two, III, A; A/CN.9/181: Yearbook . . . 1980, part two, III, B.

change and international promissory notes, articles 5 (8-10), 9(6), 11(2), 70(2, 5), 71, 72 and 74-86 as adopted by the Working Group at its eighth session (A/CN.9/WG.IV/WP.16); text of articles 25 (1) (a), 70, 74 bis, and 78 as redrafted by the Secretariat (A/CN.9/WG.IV/WP.17) and two notes by the Secretariat setting forth uniform rules applicable to international cheques (A/CN.9/WG.IV/WP.15 and 19).

### Deliberations and decisions

14. At the present session, the Working Group continued its preliminary exchange of views on articles 34 to 86 of the uniform rules applicable to international cheques, and draft articles A to F relating to crossed cheques, as drafted by the Secretariat (A/CN.9/WG.IV/WP.15 and A/CN.9/WG.IV/WP.19).

15. At the close of its session, the Working Group expressed its appreciation to the observers of member States of the United Nations and to representatives of international organizations who attended the session.

#### I. UNIFORM RULES APPLICABLE TO INTERNATIONAL CHEQUES

*Draft articles 34, X, 41-45, 53-66 bis, 67-68, 70, 70 bis, 71-72, 74, 74 bis, 74 ter, 74 quater, 78-85\**

##### *Article 34, paragraph (1)*

16. The text of article 34, paragraph (1), as considered by the Working Group, is as follows:

"(1) The drawer engages that upon dishonour of the cheque by non-payment, [and upon any necessary protest], he will pay to the holder the amount of the cheque, and any interest and expenses which may be recovered under article 67 or 68."

17. The Working Group considered the nature of the liability of the drawer on a cheque. It noted that under the provisions of the draft Convention on International Bills of Exchange and International Promissory Notes the liability of the drawer of a bill was of a secondary nature in that his liability crystallized only in the event of a due presentment of the instrument by the holder and subsequent dishonour by the drawee. The Working Group was of the view that the uniform rules applicable to international cheques should state that:

1. The undertaking of the drawer was to pay the amount of the cheque to the holder upon dishonour by non-payment;

2. The drawer of a cheque would be discharged of liability upon failure of the holder to present the cheque; in the event of delay in presentment the drawer would not be discharged except to the extent of the loss suffered because of the delay.

18. The Group was of the view that a parallel rule should apply with regard to the failure and delay in making protest.

19. The Working Group requested the Secretariat to redraft article 34, paragraph (1) accordingly.

##### *Article 34, paragraph (2)*

20. The text of article 34, paragraph (2), as considered by the Working Group, is as follows:

"(2) The drawer may not exclude or limit his own liability by a stipulation on the cheque. Any such stipulation is without effect."

21. The Working Group adopted this provision without change. One representative proposed to delete this paragraph on the ground that, in his view, a cheque on which the drawer excluded or limited his liability was not a cheque under the draft Convention.

##### *Article X*

22. The text of article X, as considered by the Working Group, is as follows:

"(1) A cheque cannot be accepted. A statement of acceptance on a cheque is without effect as an acceptance.

"(2) Any statement written on a cheque indicating certification, confirmation, acceptance, visa or any other equivalent expression has only the effect to ascertain the existence of funds and prevents the withdrawal of such funds by the drawer, or the use of such funds by the drawee for purposes other than payment of the cheque bearing such a statement, before the expiration of the time limit for presentment."

23. The Working Group noted that article X, paragraph (1), as proposed by the Secretariat, followed article 4 of the Geneva Uniform Law on Cheques in that a cheque was not capable of being accepted by the drawee and that any statement purporting to be an acceptance was without effect. The Group, after discussion, was unable to agree on a uniform rule according to which either the Geneva uniform rule should be maintained or section 3-411 of the Uniform Commercial Code of the United States of America, under which either the drawer or a holder could procure acceptance (certification), should be followed. Consequently, the Group was of the view that the proposed draft Convention should permit Contracting Parties to allow for acceptance of a cheque by a drawee-bank and, if so, to determine the legal effects thereof.

\* Each draft article is numbered to correspond to the draft article in the draft Convention on International Bills of Exchange and International Promissory Notes which relates to the same or a similar issue covered by the draft article of these uniform rules. Accordingly, when a draft article in the draft Convention has no relation to cheques, there is an interruption in the numbering sequence of the draft articles of these uniform rules, and when a draft article in these uniform rules has no relation to bills of exchange or promissory notes, it is identified by a letter (e.g. articles A to F on crossed cheques). (Footnote in original.)

24. The Working Group further noted that there existed in several countries a practice under which drawee-banks certified or confirmed a cheque or stamped a cheque with a visa. The Group was of the view that also in this respect Contracting Parties should be given the faculty to allow for such statements and to determine the legal effects thereof, as, for example, provided for under article 6 of Annex II to the Geneva Convention providing a Uniform Law on Cheques.

25. The Working Group requested the Secretariat to redraft article X accordingly.

#### Article 41

26. The text of article 41, as considered by the Working Group, is as follows:

"(1) The endorser engages that upon dishonour of the cheque by non-payment, and upon any necessary protest, he will pay to the holder the amount of the cheque, and any interest and expenses which may be recovered under article 67 or 68.

"(2) The endorser may exclude or limit his own liability by an express stipulation on the cheque. Such stipulation has effect only with respect to that endorser."

27. The question was raised whether in respect of the undertaking of the endorser to pay the cheque upon dishonour it was necessary to require also that protest be made. The Working Group, after discussion, was of the view that protest should be required because of the evidentiary effect of protest that dishonour had taken place. The Group adopted this article without change.

#### Article 42

28. The text of article 42, as considered by the Working Group, is as follows:

"(1) Any person who transfers a cheque by mere delivery is liable to any holder subsequent to himself for any damages that such holder may suffer on account of the fact that prior to such transfer

"(a) A signature on the cheque was forged or unauthorized; or

"(b) The cheque was materially altered; or

"(c) A party has a valid claim or defence against him; or

"(d) The cheque is dishonoured by non-payment.

"(2) The damages according to paragraph (1) may not exceed the amount referred to in article 67 or 68.

"(3) Liability on account of any defect mentioned in paragraph (1) is incurred only to a holder who took the cheque without knowledge of such defect."

29. The Working Group adopted this article without change.

#### Article 43, paragraph (1)

30. The text of article 43, paragraph (1), as considered by the Working Group, is as follows:

"(1) Payment of a cheque may be guaranteed, as to the whole or part of its amount, for the account of a party by any person, who may or may not have become a party, except the drawee."

31. The Working Group considered the following questions:

1. Whether payment of a cheque may be guaranteed not only for the account of a party but also for the account of a drawee;

2. Whether also the drawee could guarantee payment.

32. As to question 1, the Working Group noted that in the context of the draft Convention on International Bills of Exchange and International Promissory Notes it had decided that payment of a bill could be guaranteed for the account of the drawee. In such a case the person guaranteeing payment by the drawee became a party primarily liable.

33. The Working Group, after discussion, was of the view that the proposed draft Convention on International Cheques should not allow for a guarantee being given for the account of the drawee-bank. The Group concluded that, in the absence of evidence of a regular banking practice in this respect, it would not be justified to draw up elaborate rules on the ensuing relationship between the guarantor for the drawee and the drawee, the guarantor and the drawer, and the nature of the guarantor's liability.

34. As to question 2, the Working Group was of the opinion that article 43 should permit the drawee to become a guarantor. Consequently, the Group decided to delete the words "except the drawee" at the end of paragraph (1).

#### Article 43, paragraphs (2) and (3)

35. The text of article 43, paragraphs (2) and (3), as considered by the Working Group, is as follows:

"(2) A guarantee must be written on the cheque or on a slip affixed thereto ('*allonge*').

"(3) A guarantee is expressed by the words: 'guaranteed', '*aval*', 'good as *aval*' or words of similar import, accompanied by the signature of the guarantor."

36. The Working Group adopted these paragraphs without change.

#### Article 43, paragraph (4)

37. The text of article 43, paragraph (4), as considered by the Working Group, is as follows:

"(4) A guarantee may be effected by a signature alone. Unless the content otherwise requires

"(a) The signature alone on the front of the cheque, other than that of the drawer, is a guarantee;

"(c) A signature alone on the back of the cheque is an endorsement."

38. The Working Group adopted this paragraph without change. The question was raised whether, if by virtue of article X a State permitted acceptance of a cheque by the drawee and if in that State, under its own legislation, acceptance could be effected by the mere signature of the drawee on the face of the cheque, such signature constituted an acceptance or a guarantee for payment by the drawee. The Working Group, after discussion, was of the view that the rule set forth in paragraph (4) (a) that a signature alone on the face of the cheque, other than that of the drawer, was a guarantee should be maintained. Therefore, the signature of a drawee signing as an acceptor should only be considered to be an acceptance if that signature was accompanied by the word "accepted" or words of similar import.

39. The further question was raised as to what would be the effect of a blank signature on a cheque. The Working Group was of the view that the provision set out in paragraph (4) (c) should be maintained and that, therefore, such signature should be considered as an endorsement. As to the question whether a cheque made payable to bearer could be converted into a cheque payable to order by means of a special endorsement of the holder, the Group was of the view that, once the cheque had been made payable to bearer by the drawer, a special endorsement could not convert it into a cheque payable to the order of the named endorsee. The Working Group requested the Secretariat to draft appropriate wording, along the lines of article 20 of the Geneva Uniform Law on Cheques.

#### *Article 43, paragraph (5)*

40. Text of article 43, paragraph (5), as considered by the Working Group, is as follows:

"(5) A guarantor may specify the person for whom he has become guarantor. In the absence of such specification, the person for whom he has become guarantor is the drawer."

41. The Working Group adopted this paragraph without change.

#### *Article 44*

42. The text of article 44, as considered by the Working Group, is as follows:

"A guarantor is liable on the cheque to the same extent as the party for whom he has become guarantor, unless the guarantor has stipulated otherwise on the cheque."

43. The Working Group adopted this article without change.

#### *Article 45*

44. The text of article 45, as considered by the Working Group, is as follows:

"The guarantor who pays the cheque has rights thereon against the party for whom he became guarantor and against parties who are liable thereon to that party."

45. The Working Group adopted this article without change.

#### *Article 53*

46. The text of article 53, as considered by the Working Group, is as follows:

"A cheque is duly presented for payment if it is presented in accordance with the following rules:

"(a) The holder must present the cheque to the drawee or at a clearing-house on a business day at a reasonable hour;

"(f) A cheque must be presented for payment within . . . of its stated date;

"(g) A cheque must be presented for payment:

"(i) At the place of payment specified on the cheque; or

"(ii) If no place of payment is specified, at the address of the drawee indicated on the cheque; or

"(iii) If no place of payment is specified and the address of the drawee is not indicated, at the principal place of business of the drawee."

47. It was noted that paragraph (a) laid down that presentment of a cheque to a clearing-house was due presentment. Two questions were raised in this respect: 1. whether it should be specified that in such a case presentment was only due presentment if it was made to a clearing-house of which the drawee-bank was a member, and 2. whether, if presentment at a clearing-house was maintained, this would not have to be reflected in paragraph (g) concerning the place where the cheque must be presented for payment. The Working Group was in agreement with the substance of these observations and decided to delete in paragraph (a) the words "or at a clearing-house" and to add a new paragraph (h) to read as follows:

"(h) Presentment for payment may be made at a clearing-house of which the drawee is a member."

48. As a consequence of the rule adopted for cheques in respect of presentment at a clearing-house, the Working Group decided to make corresponding modifications to article 53 of the draft Convention on International Bills of Exchange and International Promissory Notes.

49. Concerning paragraph (f), different views were expressed as to the period of time within which a cheque



must be presented for payment. Under one view, the time-limit should be as brief as possible because a cheque was essentially a payment instrument and the rules should prevent any speculation on the part of the holder to delay presentment so as to benefit from possible currency fluctuations in his favour. Under another view, the time-limit within which presentment should be made should take into account delays due to slow means of communication and the absence in some countries of a well-developed system of collection. The Group, after discussion, considered various proposals and decided to propose in the draft rules, by way of compromise, that a cheque should be presented within 120 days of its stated date.

50. The Working Group adopted the article subject to the above modifications.

#### *Article 54, paragraph (1)*

51. The text of article 54, paragraph (1), as considered by the Working Group, is as follows:

"(1) Delay in making presentment for payment is excused when the delay is caused by circumstances which are beyond the control of the holder and which he could neither avoid nor overcome. When the cause of delay ceases to operate, presentment must be made with reasonable diligence."

52. The Working Group adopted this provision without change.

#### *Article 54, paragraph (2)*

53. The text of article 54, paragraph (2), as considered by the Working Group, is as follows:

"(2) Presentment for payment is dispensed with

"[(a) If the drawer, an endorser or guarantor has waived presentment expressly or by implication; such waiver:

"(i) If made on the cheque by the drawer, binds any subsequent party and benefits any holder;

"(ii) If made on the cheque by a party other than the drawer, binds only that party but benefits any holder;

"(iii) If made outside the cheque, binds only the party making it and benefits only a holder in whose favour it was made.]

"(c) If the cause of delay continues to operate beyond . . . , after the expiration of the time-limit for presentment for payment."

54. The Working Group adopted paragraph (2) (a) without change, maintaining the brackets.

55. It was suggested that the drawer would waive presentment by implication if he had countermanded payment. However, the contrary view was expressed that

the fact that the drawer had countermanded payment should not dispense the holder from presenting the cheque to the drawee. One representative expressed the view that a waiver of presentment on the cheque by the drawer contradicted the nature of the cheque.

56. As to paragraph (c), the Working Group decided that presentment for payment could be dispensed with if the cause of delay referred to in paragraph (1) of article 54 had continued to operate beyond thirty days.

#### *Article 55*

57. The text of article 55, as considered by the Working Group, is as follows:

"If a cheque is not duly presented for payment, the endorsers and their guarantors are not liable thereon."

58. The Working Group considered whether due presentment was necessary in order to make the drawer liable on the cheque. It was noted that under the Geneva Uniform Law on Cheques the failure of the holder to make due presentment discharged the drawer of liability on the cheque. However, article 20 of Annex II to the Geneva Convention providing a Uniform Law on Cheques permitted a High Contracting Party "not to make it a condition for the exercise of the right of recourse against the drawer that the cheque must be presented and the protest drawn up . . . and to determine the effects of this recourse."

59. Under the British Bills of Exchange Act 1882 (section 74(1)), "where a cheque is not presented for payment within a reasonable time of its issue, and the drawer or the person on whose account it is drawn had the right at the time of such presentment as between him and the banker to have the cheque paid and suffers actual damage through the delay, he is discharged to the extent of such damage, that is to say, to the extent to which such drawer or person is a creditor of such banker to a larger amount than he would have been had such cheque been paid." Therefore, under this rule, the drawer of a cheque was not discharged by mere delay in presentment except to the extent the drawer had suffered damage as a result of the delay.

60. Under the Uniform Commercial Code, section 3-502, where without excuse presentment was delayed beyond the time when it was due "any drawer who because the drawee or payor bank becomes insolvent during the delay is deprived of funds maintained with the drawee or payor bank to cover the instrument may discharge his liability by written assignment to the holder of his rights against the drawee or payor bank in respect of such funds, but such drawer is not otherwise discharged."

61. The Working Group, after discussion, was of the opinion, in view of the provisions in the various statutes referred to above, that the rule that the drawer would be discharged of liability in the event of failure by the



holder to duly present the cheque would not be justified. On the other hand, it would equally not be justified to hold the drawer liable on the cheque if no presentment had been made at all. The Group was of the view that the rule laid down in the Geneva Uniform Law on Cheques should be tempered by a provision that delay in making due presentment would not lead to the discharge of the drawer's liability, but that in such a case the drawer had a right to reduce his liability by the amount of the loss he had suffered as a consequence of the delay. Consequently the Group decided that the Secretariat, in re-drafting the provisions so as to cover the liability of the drawer, should base itself on the following principles:

1. Presentment is necessary in order to make the drawer liable on the cheque;
  2. In the absence of presentment, the drawer is discharged of liability on the cheque; and
  3. Delay in making presentment does not discharge the drawer of his liability, but if such delay had given rise to loss or damages the amount of the cheque for which the drawer is liable would be reduced by the amount of loss or damages suffered.
62. The Working Group decided that parallel rules should obtain in respect of the duty of the holder to make protest for dishonour by non-payment.

#### Article 56

63. The text of article 56, as considered by the Working Group, is as follows:

"(1) A cheque is considered to be dishonoured by non-payment

"(a) When payment is refused upon due presentment or when the holder cannot obtain the payment to which he is entitled under this Convention;

"(c) If presentment for payment is dispensed with pursuant to article 54 (2) and the cheque is unpaid.

"(2) If a cheque is dishonoured by non-payment, the holder may, subject to the provisions of article 57, exercise a right of recourse against the drawer, the endorsers and their guarantors."

64. The Working Group adopted this article without change, in the light of the debate on article 54 (2) (a).

#### Article 57

65. The text of article 57, as considered by the Working Group, is as follows:

"If a cheque has been dishonoured by non-payment, the holder may exercise a right of recourse [against the endorsers and their guarantors] only after the cheque has been duly protested for dishonour in accordance with the provisions of articles 58 to 61."

66. The Working Group adopted this article subject to the deletion of the words "against the endorsers and

their guarantors" and to aligning the provisions relating to protest for dishonour with the decision taken in respect of article 55.

#### Article 58, paragraphs (1), (2) and (3)

67. The text of article 58, paragraphs (1), (2) and (3), as considered by the Working Group, is as follows:

"(1) A protest is a statement of dishonour drawn up at the place where the cheque has been dishonoured and signed and dated by a person authorized to certify dishonour of a negotiable instrument by the law of that place. The statement must specify:

"(a) The person at whose request the cheque is protested;

"(b) The place of protest; and

"(c) The demand made and the answer given, if any, or the fact that the drawee could not be found.

"(2) A protest may be made

"(a) On the cheque itself or on a slip affixed thereto ('allonge'); or

"(b) As a separate document, in which case it must clearly identify the cheque that has been dishonoured.

"(3) Unless the cheque stipulates that protest must be made, a protest may be replaced by a declaration written on the cheque and signed and dated by the drawee; the declaration must be to the effect that payment is refused."

68. The Working Group adopted these provisions without change.

#### Article 58, paragraph (3 bis)

69. The text of article 58, paragraph (3 bis), as considered by the Working Group, is as follows:

"(3 bis) Where a cheque is presented to a clearing-house, protest may be made by a dated declaration by the clearing-house to the effect that the cheque had been presented to it and has not been paid."

70. The Working Group decided to modify this provision by substituting for the words "protest may be made" the words "protest may be replaced". The Working Group also decided that a similar provision should be inserted in the draft Convention on International Bills of Exchange and International Promissory Notes.

#### Article 58, paragraph (4)

71. The text of article 58, paragraph (4), as considered by the Working Group, is as follows:

"(4) A declaration made in accordance with paragraph (3) is deemed to be a protest for the purposes of this Convention."

72. The Working Group decided to insert in the paragraph a reference to paragraph (3 bis).

*Article 59*

73. The text of article 59, as considered by the Working Group, is as follows:

"Protest for dishonour of a cheque by non-payment must be made on the day on which the cheque is dishonoured or on one of the two business days which follow."

74. The Working Group adopted this article without change.

*Article 60*

75. The text of article 60, as considered by the Working Group, is as follows:

"(1) If a cheque which must be protested for non-payment is not duly protested, the endorsers and their guarantors are not liable thereon.

"(2) Failure to protest a cheque does not discharge the drawer or his guarantor of liability thereon."

76. The Working Group, in accordance with its decisions taken in respect of articles 34 (1) and 55, decided to delete paragraph (2) and to request the Secretariat to re-draft paragraph (1) so as to include the drawer, based on the following principles: 1. protest is necessary to charge the drawer or his guarantor; 2. the provision for late protest in such a case should be drafted in the light of the discussion on articles 34 (1) and 55.

*Article 61, paragraph (1)*

77. The text of article 61, paragraph (1), as considered by the Working Group, is as follows:

"(1) Delay in protesting a cheque for dishonour is excused when the delay is caused by circumstances which are beyond the control of the holder and which he could neither avoid nor overcome. When the cause of delay ceases to operate, protest must be made with reasonable diligence."

78. The Working Group adopted this provision without change.

*Article 61, paragraph (2)*

79. The text of article 61, paragraph (2), as considered by the Working Group, is as follows:

"(2) Protest for dishonour by non-payment is dispensed with:

"(a) If the drawer, an endorser or guarantor has waived protest expressly or by implication; such waiver:

"(i) If made on the cheque by the drawer, binds any subsequent party and benefits any holder;

"(ii) If made on the cheque by a party other than the drawer, binds only that party but benefits any holder;

"(iii) If made outside the cheque, binds only the party making it and benefits only a holder in whose favour it was made.

"(b) If the cause of delay in making protest continues to operate beyond . . . after the date of dishonour;

"[(c) As regards the drawer of a cheque, if the drawer and the drawee are the same person;]

"(e) If presentment for payment is dispensed with in accordance with article 49 (2) or 54 (2);

"(f) If the person claiming payment under article 80 cannot effect protest by reason of his inability to satisfy the requirements of article 83."

80. The Working Group adopted the substance of this paragraph subject to the following decisions:

1. In sub-paragraph (2) (b), protest for dishonour would be dispensed with if the cause of the delay referred to in paragraph (1) continued to operate beyond thirty days after the date of dishonour. It was suggested that sub-paragraph 2 (b) should become sub-paragraph (2) (a).

2. To retain the provisions of sub-paragraph (2) (c).

3. To delete in sub-paragraph (2) (e) the reference to article 49, paragraph (2).

4. To delete sub-paragraph (2) (f) (see decision below, paragraph 159).

81. In respect of sub-paragraph (2) (a), one representative reserved her position on the ground that, in her view, the possibility under that provision of protest being waived on the cheque by implication was unacceptable.

*Articles 62, 63 and 64*

82. The text of articles 62, 63 and 64, as considered by the Working Group, is as follows:

*"Article 62*

"(1) The holder, upon dishonour of a cheque by non-payment, must give due notice of such dishonour to the drawer, the endorsers and their guarantors.

"(3) An endorser or a guarantor who received notice must give notice of dishonour to the party immediately preceding him and liable on the cheque.

"(4) Notice of dishonour operates for the benefit of any party who has a right of recourse on the cheque against the party notified.

*"Article 63*

"(1) Notice of dishonour may be given in any form whatever and in any terms which identify the cheque and state that it has been dishonoured. The return of the dishonoured cheque is sufficient notice, provided it

is accompanied by a statement indicating that it has been dishonoured.

"(2) Notice of dishonour is deemed to have been duly given if it is communicated or sent to the person to be notified by means appropriate in the circumstances, whether or not it is received by that person.

"(3) The burden of proving that notice has been duly given rests upon the person who is required to give such notice.

#### *"Article 64*

"Notice of dishonour must be given within the two business days which follow

"(a) The day of protest or, if protest is dispensed with, the day of dishonour; or

"(b) The receipt of notice given by another party."

83. The Working Group adopted these articles without change.

#### *Article 65, paragraph (1)*

84. The text of article 65, paragraph (1), as considered by the Working Group, is as follows:

"(1) Delay in giving notice of dishonour is excused when the delay is caused by circumstances which are beyond the control of the holder and which he could neither avoid nor overcome. When the cause of delay ceases to operate, notice must be given with reasonable diligence."

85. The Working Group adopted this provision without change.

#### *Article 65, paragraph (2)*

86. The text of article 65, paragraph (2), as considered by the Working Group, is as follows:

"(2) Notice of dishonour is dispensed with

"(a) If [the drawer,] an endorser or guarantor has waived notice of dishonour expressly or by implication; such waiver:

"(i) If made on the cheque by the drawer, binds any subsequent party and benefits any holder;

"(ii) If made on the cheque by a party other than the drawer, binds only that party but benefits any holder;

"(iii) If made outside the cheque, binds only the party making it and benefits only a holder in whose favour it was made.

"(b) If after the exercise of reasonable diligence notice cannot be given;

"[(c) As regards the drawer of a cheque, if the drawer and the drawee are the same person.]"

87. The Working Group decided to retain the words "the drawer" occurring in paragraph (2), sub-paragraph (a).

88. One representative reserved her position on the ground that, in her view, the possibility of notice of dishonour being waived on the cheque by implication was unacceptable.

89. The Working Group adopted, subject to the decision taken in regard to the words "the drawer", the provisions of sub-paragraph (a).

90. The Working Group also decided to retain sub-paragraph (c) of paragraph (2).

#### *Articles 66 and 66 bis*

91. The text of articles 66 and 66 bis, as considered by the Working Group, is as follows:

#### *"Article 66*

"Failure to give due notice of dishonour renders a person who is required to give such notice under article 62 to a party who is entitled to receive such notice liable for any damages which that party may suffer directly from such failure, provided that such damages do not exceed the amount due under article 67 or 68.

#### *"Article 66 bis*

"The holder may exercise his rights on the cheque against any one party, or several or all parties, liable thereon and is not obliged to observe the order in which the parties have become bound."

92. The Working Group adopted these articles without change.

#### *Article 67*

93. The text of article 67, as considered by the Working Group, is as follows:

"(1) The holder may recover from any party liable the amount of the cheque with interest, if interest has been stipulated for.

"(2) When payment is made after the cheque has been dishonoured the amount of the cheque with interest, if interest has been stipulated for, from the date of dishonour to the date of payment, or, in the absence of such stipulation, interest at the rate specified in paragraph (4) calculated from the date of dishonour on the sum specified in paragraph (2).

"(3) Any expenses of protest and of the notices given by him.

"(4) The rate of interest shall be [2] per cent per annum above the official rate (bank rate) or other similar appropriate rate effective in the main domestic centre of the country where the cheque was payable, or if there is no such rate, then at the rate of [ ] per cent

per annum, to be calculated on the basis of the number of days in accordance with the custom of that centre."

94. It was recalled that, during its consideration of article 7, the Working Group had left open the question whether the proposed draft Convention should allow for the stipulation of interest on a cheque and that it had been decided to take up the matter in the context of article 67. Various views were expressed on this issue. Under one view, the proposed draft Convention should permit the stipulation of interest so that in countries where this practice existed it could continue under the Convention. In addition, the draft Convention on International Bills of Exchange and International Promissory Notes permitted the stipulation of interest on bills of exchange payable on demand.

95. The contrary view was expressed that the proposed Convention should not permit a stipulation of interest because the cheque was essentially a payment instrument and not a credit instrument. Also, in view of automated cheque processing procedures obtaining in many countries, the handling of cheques might well be hampered if banks had to calculate the amount payable because of a stipulation of interest. If a creditor wished to be paid by an instrument containing an interest-clause, he could demand a bill payable at sight drawn on a bank.

96. The Working Group, after deliberation, decided that the proposed draft Convention should not set forth a provision allowing for the stipulation of interest.

97. As a result of this decision, the Working Group decided to delete, in paragraph (1) of article 67, the words "with interest, if interest has been stipulated for".

98. In consequence of the aforementioned decision in respect of the stipulation of interest, the Working Group decided to modify paragraph (2) of article 67 accordingly. The Group further decided to replace, in this paragraph, the words "date of dishonour" by the words "date of presentment" on the following grounds. Under article 5, paragraph (9) of the draft Convention on International Bills of Exchange and International Promissory Notes the maturity date of a demand bill was the date on which the instrument was presented for payment. Under article 67, paragraph (1)(b)(ii) of the draft Convention on International Bills of Exchange and International Promissory Notes interest payable on a demand bill which had been dishonoured would run from the date of presentment. Therefore, since the cheque was a demand instrument, a similar rule should obtain in respect of cheques.

99. Consequently, the Working Group decided to replace paragraphs (2) and (3) of article 67 by the following wording:

"(2) When payment is made after the cheque has been dishonoured, the holder may recover from any party liable the amount of the cheque with interest at

the rate specified in paragraph (4) calculated from the date of presentment to the date of payment and any expenses of protest and of the notices given by him."

100. It was observed that under article 67, paragraph (1)(b) of the draft Convention on International Bills of Exchange and International Promissory Notes interest payable on a non-demand instrument would run from the date of maturity. However, in the case of parties primarily liable (acceptor and maker) this rule could give rise to unacceptable results as in the case where presentment for payment of an accepted bill or of a note was made after maturity. It was proposed, therefore, that article 67, paragraph (1)(b) should be modified so as to make interest run from the date of presentment.

101. The Working Group requested the Secretariat to prepare an explanatory memorandum setting forth the issues raised by the above proposal and to prepare, if appropriate, alternative drafts.

102. The Working Group did not retain a proposal that the proposed draft Convention on International Cheques should set forth the possibility of a stipulation on the cheque for interest payable after dishonour of the cheque.

103. The Working Group decided that paragraph (4) of article 67 be retained but that it may be re-considered at a later stage. The view was expressed that the current text might not permit in all circumstances the determination of the applicable rate of interest.

#### *Article 68*

104. The text of article 68, as considered by the Working Group, is as follows:

"(1) A party who takes up and pays a cheque in accordance with article 67 may recover from the parties liable to him

"(a) The entire sum which he was obliged to pay in accordance with article 67 and has paid;

"(b) Interest on that sum at the rate specified in article 67, paragraph (4) from the date on which he made payment;

"(c) Any expenses of the notices given by him.

"(2) . . ."

105. The Working Group adopted this article but decided to add a paragraph (2), similar to paragraph (2) of article 68 of the draft Convention on International Bills of Exchange and International Promissory Notes, reading as follows:

"(2) Notwithstanding article 25 (4), if a party takes up and pays the cheque in accordance with article 67 and the cheque is transferred to him such transfer does not vest in that party the rights to and upon the cheque which any previous protected holder had."

*Article 70, paragraphs (1) and (3)*

106. The text of article 70, paragraphs (1) and (3), as considered by the Working Group, is as follows:

"(1) A party is discharged of his liability on the cheque when he pays the holder or a party subsequent to himself the amount due pursuant to articles 67 and 68.

"(3) A party is not discharged of his liability if he knows at the time of payment that a third person has asserted a valid claim to the cheque or that the holder acquired the cheque by theft or forged the signature of the payee or an endorsee, or participated in such theft or forgery."

107. The Working Group decided to adapt the wording of these paragraphs to that of paragraphs (1) and (3) of article 70 of the draft Convention on International Bills of Exchange and International Promissory Notes which had been approved at its ninth session. Consequently, the Working Group adopted the following text:

"(1) A party is discharged of his liability on the cheque when he pays the holder or a party subsequent to himself who has taken up and paid the cheque the amount due pursuant to articles 67 and 68.

"(3) A party is not discharged of his liability if he pays a holder who is not a protected holder and knows at the time of payment that a third person has asserted a valid claim to the cheque or that the holder acquired the cheque by theft or forged the signature of the payee or an endorsee, or participated in such theft or forgery."

*Article 70, paragraph (4)*

108. The text of article 70, paragraph (4), as considered by the Working Group, is as follows:

"(4)(a) A person receiving payment of a cheque under paragraph (1) of this article must, unless agreed otherwise, deliver to the person making such payment the cheque, any protest, and a receipted account.

"(b) The person from whom payment is demanded may withhold payment if the person demanding payment does not deliver the cheque to him. Withholding payment in these circumstances does not constitute dishonour by non-payment.

"(c) If payment is made but the payor fails to obtain the cheque, the payor is discharged but the discharge cannot be set up as a defence against a protected holder."

109. It was observed that sub-paragraph (a) of paragraph (4) envisaged the situation of payment of a cheque upon dishonour. It was suggested that this provision should also deal with the obligation placed upon a person receiving payment from the drawee. The Working Group accepted this proposal and decided that a similar modifi-

cation should be made to article 70, paragraph (1) (a) of the draft Convention on International Bills of Exchange and International Promissory Notes. However, it was noted that the requirement that the person receiving payment deliver to the person paying a receipted account would only be applicable in situations where a party paid in a recourse action. The Working Group concurred with this observation and requested the Secretariat to draft separate provisions relating to payment by the drawee and payment by a party.

110. The Working Group adopted sub-paragraph (b) of paragraph (4) without change.

111. As to sub-paragraph (c), the Working Group reaffirmed its view that, where a cheque had been paid and the person paid had retained the cheque and had subsequently transferred it to a protected holder, such protected holder had a right to be paid and the defence of prior payment could not be set up against him. However, it was observed that this result already followed from article 25 relating to the rights of a protected holder and that, therefore, sub-paragraph (c) was superfluous. The Working Group concurred with this observation and noted that, if the person to whom the cheque had been transferred was not a protected holder, the defence of discharge because of payment could be set up against him (article 24). However, the Working Group requested the Secretariat to re-examine articles 24 and 25 in order to ascertain whether these results clearly emerged from the wording of these articles.

*New article 70 bis*

112. The text of article 70 bis, as considered by the Working Group, is as follows:

"If the drawee without knowledge that an endorsement is forged or is made by a person in a representative capacity without authority [or that a third person has asserted a valid claim to the cheque] pays a cheque drawn on him to the holder, he does not, in doing so, incur any liability by reason only of such forged or unauthorized endorsement [or the assertion of such claim]."

113. In examining this article, the Working Group considered the regime applicable under the draft Convention to payment of an instrument on which an endorsement had been forged. Under article 22 of the draft Convention on International Bills of Exchange and International Promissory Notes, as adopted by the Working Group, a party who has suffered damages because of the forged endorsement on a bill of exchange has a right to recover compensation from the person who forged the endorsement and from the person who took the bill directly from such person. Thus, where the bill had been stolen from the payee and the thief forged the payee's endorsement and transferred the bill to A, who received payment from the drawee, the payee had a right

to recover compensation for damages against both the thief and A, even if A was a protected holder. However, if the thief had not transferred the instrument to A but had himself received payment from the drawee, then the question arose whether the action of the payee would lie not only against the thief but also against the drawee. In other words, could the drawee be considered as a person who took the bill directly from the forger?

114. The Working Group concluded that the present wording of article 22 did not make it immediately clear whether or not article 22 extended to a person who took an instrument directly from the forger by reason of the fact that he paid the instrument. Divergent views were expressed as to what should be the proper rule.

115. Under one view, the drawee who paid a bill under a forged endorsement directly to the forger should be liable to the payee because the drawee when he takes the instrument from the forger should be in a similar position as an endorser who takes from the forger. The legal effects of such a solution would differ if the draft Convention should distinguish between payment by the drawee with knowledge and without knowledge that an endorsement was forged. New article 70 *bis*, as proposed by the Secretariat, owed its existence to this distinction in that it provided that, if the drawee paid an instrument without knowledge that an endorsement was forged, he did not incur any liability by reason only of the forged endorsement. It was suggested that thought should also be given to the appropriateness of having different rules in this respect according to whether the instrument was a bill or note or a cheque. In the case of a bill or note, the drawee or acceptor or the maker had the faculty of ascertaining to whom he paid the instrument.

116. Under another view, the drawee should not be held liable because the maxim "know your endorser", on which the right to recover compensation under article 22 was based, should not apply to the drawee. As under the first view, different rules would obtain if the draft Convention distinguished between payment by the drawee with knowledge and without knowledge that an endorsement was forged. If the drawee paid with knowledge of the forgery, he should bear the risk of loss since he paid knowingly a person who had no right to the instrument, i.e. the forger. In other words, the drawee could then not debit the drawer's account, and the drawer was not discharged. On the other hand, if the drawee paid the instrument without knowledge of the forgery, he should not bear the risk of loss but that risk should be on the payee who lost the instrument and the drawer was discharged. The view was expressed that, if this approach was adopted for bills and notes, it should also be adopted for cheques.

117. Under a third view, payment by the drawee to the forger should subject the drawee to liability to pay compensation to the payee whose signature was forged

only in the case where such payment by the drawee was made with knowledge that the signature of the payee was forged. Under this view, like under the second view, the risk of forgery would be borne by the person who lost the instrument if payment was made without knowledge of the forgery. On the other hand, if payment was made with knowledge of the forgery the risk of loss would be on the drawee. However, unlike the results obtaining under the second view, it was for purposes of discharge of the drawer immaterial whether payment by the drawee was with or without knowledge of the forgery.

118. The Working Group was of the view that the various issues raised during the discussions required further consideration. It therefore requested the Secretariat to draft alternative provisions based on the views expressed and also to take into account the issue of paid stolen bearer instruments. The Working Group also requested the Secretariat to submit an explanatory memorandum of the alternative draft provisions.

#### *Article 71, paragraph (1)*

119. The text of article 71, paragraph (1), as considered by the Working Group, is as follows:

"(1) The holder is not obliged to take partial payment."

120. The Working Group adopted this paragraph without change.

#### *Article 71, paragraph (2)*

121. The text of article 71, paragraph (2), as considered by the Working Group, is as follows:

"(2) If the holder does not take partial payment, the cheque is dishonoured by non-payment."

122. It was observed that this paragraph, though it expressed correctly the intended rule, was drafted awkwardly. The Working Group requested the Secretariat to re-draft this provision so as to express more clearly the idea that the cheque is dishonoured by non-payment if the holder who is offered partial payment does not take it.

#### *Article 71, paragraph (3)*

123. The text of article 71, paragraph (3), as considered by the Working Group, is as follows:

"(3) If the holder takes partial payment from the drawee, the cheque is to be considered as dishonoured by non-payment as to the amount unpaid."

124. The Working Group adopted this paragraph without change.

#### *Article 71, paragraph (4)*

125. The text of article 71, paragraph (4), as considered by the Working Group, is as follows:

"(4) If the holder takes partial payment from a party to the cheque other than the drawee,

"(a) The party making payment is discharged of his liability on the cheque to the extent of the amount paid; and

"(b) The holder must give such a certified copy of the cheque, and of any authenticated protest, in order to enable subsequent recourse to be exercised."

126. The Working Group adopted this paragraph subject to deleting the words "other than the drawee".

#### *Article 71, paragraph (5)*

127. The text of article 71, paragraph (5), as considered by the Working Group, is as follows:

"(5) The drawee or a party making partial payment may require that mention of such payment be made on the cheque and that a receipt therefor be given to him."

128. The following example was given: The drawer issues a cheque payable to the order of the payee, the payee endorses it to A and A to B; B presents the cheque for payment to the drawee. Upon dishonour by the drawee, B demands payment from the drawer and the drawer pays partially without requiring that mention of the partial payment be made on the cheque. Subsequently B demands payment from the payee who pays the whole amount. The question was put whether paragraph (5) should not require that mention of partial payment must be made on the cheque so as to prevent B from being paid the full amount of the cheque.

129. It was noted in this respect that normally a party paying partially would require that mention of the partial payment be made on the cheque so as to protect himself against a subsequent protected holder. Furthermore, if one were to make the mention of partial payment on the cheque obligatory, the question immediately arose what would be the sanction of non-conformity with such obligation. The Working Group, after discussion, decided to retain paragraph (5) in its present wording.

#### *Article 71, paragraph (6)*

130. The text of article 71, paragraph (6), as considered by the Working Group, is as follows:

"(6) Where a party pays the unpaid amount, the person receiving the unpaid amount who is in possession of the cheque must deliver to him the receipted cheque and any authenticated protest."

131. It was proposed that the rule set out in this paragraph should equally apply in the case where a drawee paid the unpaid amount. The Working Group accepted this proposal and requested the Secretariat to amend also paragraph (6) of article 71 of the draft Convention on International Bills of Exchange and International Promissory Notes accordingly.

#### *Article 72*

132. The text of article 72, as considered by the Working Group, is as follows:

"(1) The holder may refuse to take payment in a place other than the place where the cheque was duly presented for payment in accordance with article 53 (g).

"(2) If payment is not then made in the place where the cheque was duly presented for payment in accordance with article 53 (g), the cheque is considered as dishonoured by non-payment.

133. The Working Group adopted this article without change.

#### *Article 74*

134. The text of article 74, as considered by the Working Group, is as follows:

"(1) A cheque must be paid in the currency in which the amount of the cheque is expressed.

"(2) The drawer may indicate on the cheque that it must be paid in a specified currency other than the currency in which the amount of the cheque is expressed. In that case:

"(a) The cheque must be paid in the currency so specified;

"(b) The amount payable is to be calculated according to the rate of exchange indicated on the cheque. Failing such an indication, the amount payable is to be calculated according to the rate of exchange for sight drafts on the date of presentment:

"(i) Ruling at the place where the cheque must be presented for payment in accordance with article 53 (g), if the specified currency is that of that place (local currency); or

"(ii) If the specified currency is not that of that place, according to the usages of the place where the cheque must be presented for payment in accordance with article 53 (g).

"(c) If such a cheque is dishonoured by non-payment, the amount is to be calculated:

"(i) If the rate of exchange is indicated on the cheque, according to that rate;

"(ii) If no rate of exchange is indicated on the cheque, at the option of the holder, according to the rate of exchange ruling on the date of presentment or on the date of actual payment.

"(3) Nothing in this article prevents a court from awarding damages for loss caused to the holder by reason of fluctuations in rates of exchange if such loss is caused by dishonour for non-payment.



"(4) The rate of exchange ruling at a certain date is the rate of exchange ruling, at the option of the holder, at the place where the cheque must be presented for payment in accordance with article 53 (g) or at the place of actual payment."

135. It was observed that article 74 did not specify at what rate of exchange a cheque should be paid if it had been drawn in a currency which was not that of the place of payment but because of exchange control regulations applicable in the place of payment had to be paid in local currency. It was suggested that one way of dealing with this question would be to add under article 74 *bis* additional provisions based on the provisions of paragraph (2) (b) and (c) of article 74. The Working Group decided to reconsider this issue in the light of draft provisions to be prepared by the Secretariat. The Group noted that this issue was not only relevant to the provisions applicable to cheques but also to those applicable to bills and notes.

136. With respect to paragraph (2) (b), one representative proposed to replace the words "for sight drafts" by the word "customary" or "usual". With respect to paragraph (4), one representative proposed that the substance of this paragraph should be accommodated within the provision of paragraph (2) (c) of article 74 which should also reflect the provision of paragraph (2) (b). The Working Group requested the Secretariat to take this proposal into consideration when redrafting article 74.

137. The Working Group adopted article 74 subject to the above considerations.

#### *Article 74 bis*

138. The text of article 74 *bis*, as considered by the Working Group, is as follows:

"Nothing in this Convention prevents a Contracting State from enforcing exchange control regulations applicable in its territory, including regulations which it is bound to apply by virtue of international agreements to which it is a party."

139. The Working Group adopted this article without change. But it was noted that there might be provisions of mandatory law unconnected with exchange control which should be accommodated.

#### *New article 74 ter*

140. The text of article 74 *ter*, as considered by the Working Group, is as follows:

"If the drawer countermands the order to the drawee to pay a cheque drawn on him, [the drawee is under a duty not to pay]

"[the drawee has the option either to pay or not to pay until the time-limit for presentment of the cheque has expired. After the expiration of the time-limit for presentment the drawee is under a duty not to pay.]"

141. The Working Group considered the question whether the proposed draft Convention should set forth a rule on countermand. The Group noted that all legal systems contained such a rule though the legal effects of countermand were different. It would therefore be justified that the proposed draft Convention set forth a uniform rule on countermand of payment.

142. The Working Group expressed its preference for the rule that, where the drawer had countermanded his order to the drawee to pay a cheque drawn on him, the drawee was under a duty not to pay. The alternative rule proposed by the Secretariat, namely that upon countermand the drawee had the option either to pay or not to pay the cheque, did not commend itself in that it did not bring about the required degree of uniformity. The Working Group requested the Secretariat to specify in the commentary that a countermand once notified to the drawee remained effective until revoked by the drawer.

#### *New article 74 quater*

143. The text of article 74 *quater*, as considered by the Working Group, is as follows:

"[If the drawee receives notice of the death of the drawer the drawee is under a duty not to pay.]

"[The death of the drawer does not affect the order to pay contained in the cheque drawn by him.]"

144. The Working Group considered the question whether the proposed draft Convention should set forth a provision governing the duty of the drawee not to pay a cheque upon notice of the death of the drawer. It was noted that a similar question as to the duty of the drawee would arise in cases where the drawer had become insolvent or incapacitated or where a corporation which had drawn a cheque was in liquidation. The Working Group, after discussion, was of the view that these questions should be left to national law and that, therefore, the proposed draft Convention should not set forth a specific provision in this respect. However, the observer of the Hague Conference on Private International Law indicated his willingness to prepare a short study on the conflicts aspects of this issue which could assist the Working Group in deciding whether the proposed draft Convention should contain a provision on the applicable law.

#### *Article 78*

145. The text of article 78, as considered by the Working Group, is as follows:

"(1) When a party is discharged wholly or partly of his liability on the cheque, any party who has a right of recourse against him is discharged to the same extent.



"(2) Payment of a cheque by the drawee to the holder of the amount due in whole or in part discharges all parties to the cheque to the same extent."

146. The Working Group adopted this article without change.

#### Article 79

147. The text of article 79, as considered by the Working Group, is as follows:

"(1) A right of action arising on a cheque can no longer be exercised after [four] years have elapsed

"[(a) Against the drawer or his guarantor, after the date of presentment;]

"(b) Against [the drawer or] an endorser or [their] his guarantor, after the date of protest for dishonour or, where protest is dispensed with the date of dishonour.

"(2)(a) If a party has taken up and paid the cheque in accordance with article 67 or 68 within one year before the expiration of the period referred to in paragraph (1) of this article, such party may exercise his right of action against a party liable to him within [one year] after the date on which he took up and paid the cheque;

"(b) (for subsequent consideration)."

148. It was observed that article 79 was patterned on article 79 of the draft Convention on International Bills of Exchange and International Promissory Notes. In examining the original provision, it was noted that it did not provide for a limitation period in respect of rights of action arising on a note payable on demand. The Working Group was of the view that the liability of the maker on the note existed from the date of the note. Therefore, the right of action arising on a demand note against the maker would lapse after four years from such date. In respect of a bill payable on demand which had been accepted, the period during which a right of action could be exercised against the acceptor should run from the date on which the bill had been accepted. The Working Group requested the Secretariat to amend article 79 of the draft Convention on International Bills of Exchange and International Promissory Notes accordingly.

149. As to the period during which a right of action arising on a cheque could be exercised, the Working Group was of the view that, for the sake of uniformity, the four-year period should be retained. With regard to the period during which a right of action against the drawer could be exercised, the Working Group considered two proposals. Under one proposal, a right of action could no longer be exercised after four years had elapsed after the date of presentment or after four years and 120 days had elapsed after the date of the cheque, whichever was earlier. Thus, the period of limitation would, in fact, be four years after the date of present-

ment if presentment had been made within the period of 120 days within which a cheque must be presented and would be four years and 120 days after the date of the cheque if no presentment had been made within the period of 120 days. Under the second proposal considered by the Working Group, article 79 should set forth a limitation period of four years from the date of the cheque. The Group was of the view that, though the first proposal was consistent with underlying principles of liability, the second proposal had the advantage of being simpler to apply in practice. The Working Group, after discussion, decided to adopt a limitation period of four years from the date of the cheque.

150. The Working Group adopted the provision of paragraph (1)(b) of article 79 under which a right of action against an endorser could no longer be exercised after four years had elapsed after the date of protest for dishonour or, where protest was dispensed with, the date of dishonour.

151. The Working Group adopted the provision contained in paragraph (2)(a), to become paragraph (2), and retained the words "one year" which had been placed between brackets.

#### Article 80

152. The text of article 80, as considered by the Working Group, is as follows:

"(1) When a cheque is lost, whether by destruction, theft or otherwise, the person who lost the cheque has, subject to the provisions of paragraphs (2) and (3) of this article, the same right to payment which he would have had if he had been in possession of the cheque. The party from whom payment is claimed cannot set up as a defence against liability on the cheque the fact that the person claiming payment is not in possession thereof.

"(2)(a) The person claiming payment of a lost cheque must state in writing to the party from whom he claims payment:

"(i) The elements of the lost cheque pertaining to the requirements set forth in article 1(2); these elements may be satisfied by presenting to that party a copy of that cheque;

"(ii) The facts showing that, if he had been in possession of the cheque, he would have had a right to payment from the party from whom payment is claimed;

"(iii) The facts which prevent production of the cheque.

"(b) The party from whom payment of a lost cheque is claimed may require the person claiming payment to give security in order to indemnify him for any loss which he may suffer by reason of the subsequent payment of the lost cheque.

"(c) The nature of the security and its terms are to be determined by agreement between the person claiming payment and the party from whom payment is claimed. Failing such an agreement, the Court may determine whether security is called for and, if so, the nature of the security and its terms.

"(d) If the security cannot be given, the Court may order the party from whom payment is claimed to deposit the amount of the lost cheque, and any interest and expenses which may be claimed under articles 67 and 68, with the Court or any other competent authority or institution, and may determine the duration of such deposit. Such deposit is to be considered as payment to the person claiming payment.

"New (3) The person claiming payment of a lost cheque in accordance with the provisions of this article need not give security to the drawer who has inserted in the cheque, or to an endorser who has inserted in his endorsement, such words as 'not negotiable', 'not transferable', 'not to order', 'pay (x) only', or words of similar import."

153. The Working Group adopted paragraphs (1) and (2) of this article without change but did not retain new paragraph (3) since under paragraph (2)(c) the Court could determine whether security was called for in cases provided for in new paragraph (3) and in other similar cases.

#### Article 81

154. The text of article 81, as considered by the Working Group, is as follows:

"(1) A party who has paid a lost cheque and to whom the cheque is subsequently presented for payment by another person must notify the person to whom he paid of such presentment.

"(2) Such notification must be given on the day the cheque is presented for payment or on one of the two business days which follow and must state the name of the person presenting the cheque and the date and place of presentment.

"(3) Failure to notify renders the party who has paid the lost cheque liable for any damages which the person whom he paid may suffer from such failure, provided that the total amount of the damages does not exceed the amount of the cheque and any interest and expenses which may be claimed under article 67 or 68.

"(4) Delay in giving notice is excused when the delay is caused by circumstances which are beyond the control of the person who has paid the lost cheque and which he could neither avoid nor overcome. When the cause of delay ceases to operate, notice must be given with reasonable diligence.

"(5) Notice is dispensed with when the cause of delay in giving notice continues to operate beyond 30 days after the last date on which it should have been given."

155. The Working Group adopted this article without change.

#### Article 82

156. The text of article 82, as considered by the Working Group, is as follows:

"(1) A party who has paid a lost cheque in accordance with the provisions of article 80 and who is subsequently required to, and does, pay the cheque, or who loses his right to recover from any party liable to him and such loss of right was due to the fact that the cheque was lost, has the right

"(a) If security was given, to realize the security; or

"(b) If the amount was deposited with the Court or other competent authority, to reclaim the amount so deposited.

"(2) The person who has given security in accordance with the provisions of paragraph (2)(b) of article 80 is entitled to reclaim the security when the party for whose benefit the security was given is no longer at risk to suffer loss because of the fact that the cheque is lost."

157. The Working Group adopted this article subject to replacing, for the sake of clarity, in paragraph (1) the words "who loses" by the words "who then loses".

#### Article 83

158. The text of article 83, as considered by the Working Group, is as follows:

"A person claiming payment of a lost cheque duly effects protest for dishonour by non-payment by the use of a writing that satisfies the requirements of article 80, paragraph (2)(a)."

159. The Working Group adopted the article without change. The question was raised whether article 61(2)(f), according to which protest for dishonour by non-payment is dispensed with if the person claiming payment under article 80 cannot effect protest by reason of his inability to satisfy the requirements of article 83, was justified in view of the fact that such person must, according to article 80(2)(a), satisfy these very requirements in order to be able to utilize the provisions concerning lost instruments. The Working Group was of the view that the provision of article 61(2)(f) contradicted the provisions of article 80(2)(a) and decided, therefore, to delete article 61(2)(f) of the proposed draft Convention on International Cheques and also of the draft Convention on International Bills of Exchange and International Promissory Notes.

*Article 84*

160. The text of article 84, as considered by the Working Group, is as follows:

"A person receiving payment of a lost cheque in accordance with article 80 must deliver to the party paying the writing required under paragraph (2) (a) of article 80 receipted by him and any protest and a receipted account."

161. The Working Group adopted this article without change.

*Article 85*

162. The text of article 85, as considered by the Working Group, is as follows:

"(a) A party who paid a lost cheque in accordance with article 80 has the same rights which he would have had if he had been in possession of the cheque.

"(b) Such party may exercise his rights only if he is in possession of the receipted writing referred to in article 84."

163. The Working Group adopted this article without change.

*Draft articles A to F (crossed cheques)*

164. The Working Group decided that the proposed draft Convention on International Cheques should contain provisions on crossed cheques and considered the draft articles on crossed cheques (A to F) prepared by the Secretariat.

*Article A, paragraph (a)*

165. The text of article A, paragraph (a), as considered by the Working Group, is as follows:

"(a) A cheque is crossed when it bears across its face two parallel [transverse] lines."

166. The Working Group adopted this paragraph subject to retaining the word "transverse" which had been placed between brackets. It was understood that the term "transverse lines" included perpendicular, but not horizontal lines.

*Article A, paragraph (b)*

167. The text of article A, paragraph (b), as considered by the Working Group, is as follows:

"(b) A crossing is general if it consists of the two lines only or if between the two lines the word 'banker' or an equivalent term [or the words 'and company' or any abbreviation thereof] is inserted; it is special if the name of a banker is so inserted."

168. The Working Group adopted this paragraph subject to maintaining the words "or the words 'and

company' or any abbreviation thereof" which had been placed between brackets. It was noted that such a general crossing was used in the United Kingdom and certain other Commonwealth countries.

*Article A, paragraph (c)*

169. The text of article A, paragraph (c), as considered by the Working Group, is as follows:

"(c) A cheque may be crossed generally or specially by the drawer or the holder."

170. The Working Group adopted this paragraph without change. The question was raised whether the guarantor of the drawer or of the endorser should have the faculty of crossing a cheque. The Working Group, after discussion, was of the opinion that a guarantor should not have this faculty.

*Article A, paragraphs (d), (e) and (f)*

171. The text of article A, paragraphs (d), (e) and (f), as considered by the Working Group, is as follows:

"(d) The holder may convert a general crossing into a special crossing.

"(e) A special crossing may not be converted into a general crossing.

"(f) The banker to whom a cheque is crossed specially may again cross it specially to another banker for collection."

172. The Working Group adopted these paragraphs without change.

173. The Working Group did not retain a proposal to add to article A a further paragraph according to which a banker receiving for collection an uncrossed cheque or a cheque crossed generally may cross it specially to himself. It was noted that in such a case the cheque would often have been endorsed and, thus, the banker become a holder. Where a collecting bank that was not a holder crossed it to itself, it did so as an agent of the holder.

*Article B*

174. The text of article B, as considered by the Working Group, is as follows:

"If a cheque shows on its face the obliteration either of a crossing or of the name of the banker to whom it is crossed,

"[the obliteration is regarded as not having taken place]

"[the rules on material alteration apply]."

175. The Working Group noted that the proposed text presented two different approaches to the question as to what would be the effect of an obliteration of a

crossing or of the name of the banker to whom the cheque was crossed. Under the approach taken by article 37 of the Geneva Uniform Law on Cheques the obliteration was regarded as not having been made. The view was expressed that this approach might lead to practical difficulties in that it was not in all circumstances possible for the paying banker to discern from the face of the cheque the name of the original banker to whom the cheque had been crossed. Under the approach of the British Bills of Exchange Act 1882 (section 78) the crossing on a cheque was considered a material part of the cheque and, therefore, its obliteration was considered to be a material alteration.

176. The Working Group, while recognizing the logic of the approach of the Bills of Exchange Act, was of the view that it would be difficult, if not impossible, to apply to the obliteration of a crossing the rules on material alteration set forth in article 29. The Group, after discussion, decided to follow the Geneva approach and, therefore, to retain the words "the obliteration is regarded as not having taken place" which had been placed between brackets and not to retain the second alternative relating to material alteration.

#### *Article C, paragraph (1)*

177. The text of article C, paragraph (1), as considered by the Working Group, is as follows:

"(1)(a) A cheque which is crossed generally is payable only to a banker or to a customer of the drawee.

"(b) A cheque which is crossed specially is payable only to the banker to whom it is crossed or, if such banker is the drawee, to his customer.

"(c) A banker may take a crossed cheque only from his customer or from another banker."

178. The Working Group adopted this paragraph without change.

#### *Article C, paragraph (2)*

179. The text of article C, paragraph (2), as considered by the Working Group, is as follows:

"(2) The drawee who pays or the banker who takes a crossed cheque in violation of the provisions of paragraph (1) of this article incurs liability for any damages which a person may have suffered as a result of such violation, provided that such damages do not exceed the amount due under article 67 or 68."

180. The Working Group adopted this paragraph subject to replacing the words "due under article 67 or 68" by the words "of the cheque".

#### *Article D*

181. The Working Group decided to adjourn consideration of this article until the re-consideration of article 70 *bis*.

#### *Article E*

182. The text of article E, as considered by the Working Group, is as follows:

"[If the crossing on a cheque contains the words 'not negotiable' the transferee becomes a holder but cannot become a protected holder in his own right.]"

183. The Working Group decided to retain this article. It was noted that a crossing containing the words "not negotiable" was frequently found in the banking practice of common law countries.

184. The following questions were raised: What was the legal effect of:

1. A statement on the cheque that it was not negotiable without there being a crossing?

2. A statement on the cheque that it was not negotiable and the cheque was crossed but the crossing did not contain these words?

3. A crossing on a cheque containing the words "not transferable", "pay (x) only" or words of similar import?

185. As to question 1, according to article 16 the transferee would not become a holder except for purposes of collection. As to question 2, the same legal effect would obtain. As to question 3, the Working Group was of the view that the proposed draft Convention should not deal with this question; therefore, article E would not apply to such a crossing and under article 16 the transferee would not become a holder except for purposes of collection.

#### *Article F, paragraph (1)*

186. The text of article F, paragraph (1), as considered by the Working Group, is as follows:

"[(1)(a) The drawer or the holder of a cheque may prohibit its payment in cash by writing [transversally] across the face of the cheque the words 'payable in account' or words of similar import.

"(b) In such a case the cheque can only be paid by the drawee by means of a book-entry.]"

187. The Working Group decided to retain this paragraph on the ground that the practice of making a cheque payable by a book-entry only, by means of a statement on the cheque that it is payable in account, was found in a number of countries. The Group also decided to retain, in paragraph (1)(a), the word "transversally" which had been placed between brackets.

*Article F, paragraph (2)*

188. The text of article F, paragraph (2), as considered by the Working Group, is as follows:

"[(2) The drawee who pays such a cheque other than by means of a book-entry incurs liability for any damages which a person may have suffered as a result thereof, provided that such damages do not exceed the amount due under article 67 or 68.]"

189. The Working Group decided to retain this paragraph subject to replacing the words "due under article 67 or 68" by the words "of the cheque".

190. The Working Group accepted a proposal that article F should contain a further paragraph dealing with the legal effects of an obliteration of the words "payable in account". The Group adopted the following paragraph:

"(3) If a cheque shows on its face the obliteration of the words 'payable in account', the obliteration is regarded as not having taken place."

*Legal issues arising outside the cheque*

191. The Working Group, at its ninth session, had requested the Secretariat to study legal issues arising outside the cheque and to report to it. The following issues were submitted by the Secretariat and discussed by the Working Group at its tenth session.

*A. Relationship between drawer and drawee-bank*

192. It was noted that this relationship was primarily of a contractual nature and was founded wholly or in part on the customs and usages of banks, on general conditions or on private agreements between bank and customer. Though the determination of the legal nature of the relationship between bank and customer had in most jurisdictions important legal consequences (such as the ownership of the funds deposited with the bank), the Working Group decided that the proposed draft Convention should not deal with this issue.

*B. Bank's duty to honour cheques*

193. The primary feature of the contract between bank and customer was the duty of the drawee-bank to honour cheques drawn on it by the customer (drawer). Payment of a cheque out of funds previously deposited or out of credit-lines entitled the bank to debit its customer's account. The Working Group noted that the negotiable instruments law in some countries established a liability of the drawee-bank to the drawer for damages resulting from the inexecution of the drawer's order and slander of credit where the bank wrongfully dishonoured a cheque. The Working Group, after discussion, was of the view that the proposed draft Convention should not set forth a provision in this respect.

*C. Availability of funds*

194. The Working Group considered the question whether the funds available for payment should be available at the time the cheque was issued or at the time of the bank's decision to pay or to dishonour the cheque. It was noted that article 5 of Annex II to the Geneva Convention providing a Uniform Law on Cheques left to High Contracting Parties the determination of the moment at which the drawer must have funds available with the drawee and that the Uniform Law itself was silent on that point. Article 3 of the Geneva Uniform Law on Cheques merely stated that "a cheque must be drawn on a banker holding funds at the disposal of the drawer and in conformity with an agreement, express or implied, whereby the drawer is entitled to dispose of those funds by cheque". The Working Group was of the view that the proposed draft Convention should not deal with this question.

*D. Obligation of the drawer to provide cover*

195. It was noted that cover ("*provision*") resulted from funds that the drawee held at the disposal of the drawer or from a credit which the drawee had extended to the drawer. It was also noted that many legislations provided for civil or penal sanctions in cases where a cheque was drawn on insufficient funds. The Working Group was of the view that the question whether any, and if so which, sanctions should be laid down in the case of cheques drawn on insufficient funds should be left to national law.

196. In this connexion, it was observed that under the Geneva Uniform Law on Cheques (article 3) absence of cover did not affect the validity of the instrument as a cheque. The question was raised whether, if the proposed draft Convention did not set forth a similar provision and if a State which had ratified the Convention denied the validity of a cheque drawn on insufficient funds, an international cheque would suffer the same fate in that country. The Working Group was of the view that the proposed draft Convention should contain a provision which would make it clear that absence of cover does not affect the validity of the instrument as a cheque.

*E. Duty of collecting bank to protest and send notice of dishonour*

197. It was noted that section 4-202 of the Uniform Commercial Code of the United States of America stated the basic responsibilities of a collecting bank. Amongst these responsibilities was the duty of a collecting bank to use ordinary care in sending notice of dishonour and making or providing for any necessary protest. It was observed that, in view of the short period of time within which protest must be made under the draft Convention and in view of the consequences of unexcused failure to protest, the duty of collecting banks in this respect

assumed a certain importance. However, the Working Group was of the view that the making of protest and sending of notice of dishonour was part of the customs and practices of collecting banks as reflected in the rules of the International Chamber of Commerce on the collection of commercial paper. The Working Group, therefore, concluded that it was not necessary to set forth any specific rules in this respect.

#### *F. Final payment of an instrument by the drawee-bank*

198. It was noted that section 4-213 of the Uniform Commercial Code set forth rules which defined what action with respect to an item constituted final payment. Under the Uniform Commercial Code, final payment of an item was important in that it was one of several factors which determined such questions as the effectiveness of notices, stop-orders and set-offs, and the point at which the provisional settlement of an item became final. The Working Group decided that the proposed draft Convention should not deal with these issues.

#### *G. Customer's duty to discover and report unauthorized or forged signatures and material alterations*

199. The Working Group considered the question of contributory negligence on the part of the drawer or a person from whom the cheque had been stolen. It was noted that the Uniform Commercial Code contained in section 3-406 a provision in respect of negligence contributing to material alteration or unauthorized signing. The Working Group was of the view that the principles of general law should apply and the question, therefore, be left to national law, whether legislation or case law.

#### *Post-dated cheques*

200. It was noted that under article 1 of the proposed draft Convention a cheque was an instrument payable on demand and that one of the formal requirements of a cheque was that it be dated. The question was raised what would be the legal effect of a cheque which was post-dated and, in particular, whether the refusal of the drawee-bank to pay a cheque before its stated date was to be considered as a dishonour. The Working Group was agreed that the fact that a cheque was post-dated or ante-dated did not invalidate the instrument as a cheque. Different views were expressed with respect to the question whether refusal by the drawee-bank to pay a cheque before its stated date amounted to dishonour.

201. Under one view, since the cheque was a demand instrument the holder was entitled to disregard the date written on the cheque and, consequently, a refusal by the drawee-bank to pay on demand constituted dishonour by non-payment. Furthermore, where the drawee-bank paid the cheque before its stated date, parties liable on the

cheque would be discharged. This was so although presentment of the cheque by the holder before the stated date could constitute a violation of the agreement between the drawer and the payee.

202. Under another view, the drawing of post-dated cheques occurred not infrequently and corresponded to commercial practices. The expectation of the parties was that the time-limit when a cheque was payable was determined by the stated date. Therefore, non-payment on presentment before the stated date did not constitute dishonour since the instrument was in accordance with the agreement of the parties not payable at such date of presentment.

203. Proponents of both views were, however, agreed that the question whether the drawee-bank could in such a case debit the account of the drawer was governed by the contract between the drawee-bank and its customer. The Working Group requested the Secretariat to prepare alternative drafts corresponding to the views expressed by members and observers of the Working Group.

#### *Other issues*

204. Reference was made to article 32 (2) of the Geneva Uniform Law on Cheques according to which, if a cheque has not been countermanded, the drawee may pay it even after the expiration of the time-limit for presentment. The question was raised whether under the draft Convention the drawee-bank which paid a cheque after the expiration of the time-limit for presentment (120 days) paid validly and could debit the account of the drawer. The Working Group was of the view that it followed from the provision relating to the liability of the drawer, according to which a late presentment was necessary to charge the drawer, that payment by the drawee-bank upon late presentment entitled the drawee-bank to debit the drawer's account. On the other hand, if the drawee-bank paid after the expiration of the limitation period obtaining as between the holder and the drawer, the question whether the drawee-bank was entitled to debit the drawer's account was governed by the agreement between the drawee-bank and the drawer.

205. The question was raised whether, where the bank upon presentment of the cheque did not pay immediately but consulted its customer (the drawer), such absence of immediate payment constituted dishonour. It was stated in reply that it was irrelevant for purposes of dishonour that the bank did not pay immediately because it wished to consult its customer.

206. The question was raised whether, where a holder upon due presentment of a cheque demanded payment over the counter and the drawee-bank refused to pay in cash but instead offered, for instance, to credit the account of the holder, such refusal constituted dishonour by non-payment. It was stated in reply that such refusal



constituted a dishonour because the holder was entitled to receive payment in money.

207. The question was raised whether a bank on which a cheque was drawn by another bank with which it had made appropriate arrangements could justifiably dishonour a cheque if it had not been advised by the drawing bank of the drawing of such cheque at the time of presentment. It was stated in reply that this depended on the agreement between the banks concerned and was in any event an issue arising outside the law on cheques.

## II. FUTURE WORK

208. The Working Group noted that the Commission at its thirteenth session had authorized the Group to hold a further session if required in the course of 1981. The Group was of the view that one further session would be required to consider in second reading the draft uniform rules on international cheques. It therefore decided to hold its eleventh session in New York from 3 to 14 August 1981.

209. Having regard to the work still to be accomplished, the Working Group was of the view that it will probably be able, at its eleventh session, to terminate the work on international negotiable instruments which the Commission conferred on it by its decisions made at its fifth session (1972) and its twelfth session (1979).

210. At its fifth session the Commission also requested the Working Group to consider whether the drawing up of uniform rules applicable to international cheques would best be achieved by extending the application of the draft Convention on International Bills of Exchange and International Promissory Notes for international cheques, or by drawing up a separate text on international cheques. The Working Group considered this issue at its ninth and tenth sessions, and expresses the following opinion: The Working Group notes that although there is considerable similarity between the law governing bills of exchange and promissory notes on the one hand, and cheques on the other, there are inherent in the use of cheques special features which distinguish these instruments from bills of exchange and promissory notes. One important feature is that the bill of exchange and promissory note are primarily credit instruments and that the essential feature of the cheque is that it is a payment instrument. Moreover, in civil law countries the bill of exchange and promissory note on the one hand, and the cheque on the other, are traditionally seen as different instruments and are traditionally governed by separate legal texts. The Working Group therefore suggests to the Commission that it should agree on the adoption of two separate draft texts, one setting forth uniform rules on international bills of exchange and

another setting forth uniform rules applicable to international cheques. However, it could be left to later decisions whether these separate sets of rules should be incorporated, in separate parts, in one Convention, or whether they should be set forth in two Conventions. One representative requested that there be prepared a combined text of both drafts, for working purposes only.

211. The Working Group heard a statement by the Secretary of the Commission in respect of possible courses of action which the Commission might wish to discuss when deciding upon its own work in respect of the draft texts drawn up by the Working Group, and when making recommendations in due course to the General Assembly. He noted that in view of the technical complexity of the subject-matter, substantive consideration of the texts prepared by the Working Group in the Commission and subsequently in a Diplomatic Conference to be convened by the General Assembly would in all likelihood require a period of time far in excess of the time allotted in the past to the conclusion of such conventions as the Convention on the Limitation Period in the International Sale of Goods, the United Nations Convention on the Carriage of Goods by Sea, 1978, and the United Nations Convention on Contracts for the International Sale of Goods. Consequent upon the length of time needed for the successful conclusion of a convention or conventions in the area of international negotiable instruments, there would be a substantially increased financial implication to the United Nations. Therefore, thought could be given to the advisability of adopting other appropriate procedures which would, whilst not affecting the quality of the work, reduce the period of time needed for the conclusion of such a convention or conventions. The Secretary of the Commission, without foreclosing other possible procedures, and subject to further consideration, referred to the possibility of simplifying the procedures traditionally followed for the adoption of United Nations Conventions. He informed the Working Group that he intended to consult with the Legal Counsel of the United Nations about the possibilities which might be open to the Commission in this respect, and would submit a note on this issue to the Commission at its next session.

212. The Working Group noted that it would accord with past practice for the Secretary-General to transmit the draft texts adopted by the Working Group upon their completion, together with a commentary, to Governments and interested international organizations for comments.

213. In this connexion, the Working Group suggests to the Commission that, at the appropriate time, it might wish to consider, in the light of the comments received, whether, for purposes of accelerating the work, it should request the Working Group to study and consider those comments and report to the Commission.

## B. Note by the Secretary-General: electronic funds transfer (A/CN.9/199)\*

1. The Commission, at its eleventh session, included as an item in its programme of work the legal problems arising out of electronic funds transfer.<sup>1</sup> At its twelfth session the Commission noted that the UNCITRAL Study Group on International Payments, a consultative body composed of representatives of banking and trade institutions, was engaged in studying the question.<sup>2</sup> At its thirteenth session the Commission requested the Secretariat to submit to it at its fourteenth session a progress report on the matter, so that it might give directions on the scope of further work after having considered the Study Group's conclusions.<sup>3</sup>

2. The Study Group made a preliminary study of some of the legal aspects of electronic funds transfer at its meetings in September 1978 and April 1979. The Study Group considered that its work should be expanded to reflect the best available practical experience of setting up and operating electronic payment systems. Therefore, it requested the Secretariat to solicit such information by means of a questionnaire to be circulated to central banks and other appropriate organizations.

3. The questionnaire was sent on 19 March 1980. The Study Group had before it at its meeting at Toronto, Canada, from 23 to 27 June 1980, a number of replies which had already been received. However, since additional replies were expected, it was decided that an analysis of replies should be prepared by the Secretariat for the next meeting of the Study Group at which time more definite conclusions might be reached.<sup>4</sup>

4. The next meeting of the Study Group is scheduled to be held at Munich from 17 to 21 August 1981 at which time the analysis of replies to the questionnaire will be considered. In certain respects the replies will be supplemented by information drawn from the publication entitled "Payment Systems in Eleven Developed Countries" prepared for the Bank for International Settlements by the Group of Computer Experts of the Central Banks of the Group of Ten Countries and Switzerland.

5. Since the Study Group will not have met between the thirteenth and fourteenth sessions of the Commission, the Secretariat is unable to submit to the Commission at this time any information in addition to that previously submitted which would aid the Commission in giving directives on the scope of further work.

6. The Secretariat will request the Study Group at its meeting in August to recommend to the Commission whether the Commission should undertake substantive work in this field at the present time and, if so, what the nature of that work might be. The Secretariat will submit the recommendation of the Study Group to the Commission at its next session.

### ANNEX

#### Institutions which replied to questionnaire on electronic funds transfer systems

1. Reserve Bank of Australia
2. Creditanstalt-Bankverein, Austria
3. Canadian Bankers' Association
4. State Bank of Czechoslovakia
5. National Bank of Denmark
6. Finland Bank
7. Bank of France
8. Deutsche Bank, Germany, Federal Republic of
9. National Bank of Hungary
10. Bank of Italy
11. Central Bank of Jordan
12. Central Bank of Kuwait
13. Netherlands Bank
14. Databank Systems Limited, New Zealand
15. Bank of Norway
16. Bank of Portugal
17. Bank of Sweden
18. Bankers' Automated Clearing Services Ltd., United Kingdom
19. Federal Reserve Bank of New York, United States of America

\* 29 April 1981. Referred to in Report, para. 34 (part one, A, above).

<sup>1</sup> Report of the United Nations Commission on International Trade Law on the work of its eleventh session, *Official Records of the General Assembly, Thirty-third Session, Supplement No. 17 (A/33/17)*, para. 67 (Yearbook . . . 1978, part one, II, A).

<sup>2</sup> Report of the United Nations Commission on International Trade Law on the work of its twelfth session, *Official Records of the General Assembly, Thirty-fourth Session, Supplement No. 17 (A/34/17)*, para. 55 (Yearbook . . . 1979, part one, II, A).

<sup>3</sup> Report of the United Nations Commission on International Trade Law on the work of its thirteenth session, *Official Records of the General Assembly, Thirty-fifth Session, Supplement No. 17 (A/35/17)*, para. 163 (Yearbook . . . 1980, part one, II, A).

<sup>4</sup> The list of organizations which submitted replies to the questionnaire is contained in an annex to this note.

## C. Report of the Secretary-General: universal unit of account for international conventions (A/CN.9/200)\*

1. At its eleventh session the Commission adopted the proposal of the delegation of France that the Commission "should study ways of establishing a system for determining a universal unit of constant value which

would serve as a point of reference in international conventions for expressing amounts in monetary terms."<sup>1</sup>

<sup>1</sup> A/CN.9/156; Report of the United Nations Commission on International Trade Law on the work of its eleventh session, *Official Records of the General Assembly, Thirty-third Session, Supplement No. 17 (A/33/17)*, para. 67 (Yearbook . . . 1978, part one, II, A).

\* 12 May 1981. Referred to in Report, para. 25 (part one, A, above).



2. The proposal was examined by the UNCITRAL Study Group on International Payments at its meetings in 1978, 1979 and 1980. The Study Group was of the view that the most desirable approach was to combine the use of the special drawing right (SDR) with a suitable index which would preserve over time the purchasing power of the monetary values set forth in the international conventions in question.

3. In an annex to this report a note prepared by the staff of the International Monetary Fund (IMF) at the request of the Commission's Secretariat sets forth many of the considerations which led to this recommendation. The IMF note also suggests that for most purposes a consumer price index would be suitable. It recognizes, however, that it would be possible to specify any of a number of other price indices—producer prices, export prices, GNP deflators, etc.—in the text of a convention if that were found to be preferable. In an annex to the IMF note is given the formula for the calculation of the index, this formula being the same no matter which index was chosen. The note concludes by saying that if the SDR in conjunction with a suitable SDR price index were chosen as a unit of account for use in international conventions, the necessary data would be published in the monthly IMF publication *International Financial Statistics*.

4. The SDR is now well accepted as the unit of account in international conventions of world-wide application. In spite of some criticism<sup>2</sup> and of certain problems encountered in respect of States which are not members of the IMF, the formula used in the United Nations Convention on the Carriage of Goods by Sea, 1978\* is essentially the same as that used in other conventions and draft conventions.<sup>3</sup> Therefore, the only new element in this proposal is that the purchasing power of sums specified in SDRs in such conventions be maintained through the use of a suitable price index.

5. The technical problems of drafting such a provision are minimal. The major policy question would be the particular price index to be used, but that decision could be left until the draft provision was before the Commission for adoption since all of the other policy and drafting questions would be the same no matter which price index were chosen.<sup>4</sup>

6. Since provisions based upon the formula used in the United Nations Convention on the Carriage of Goods by Sea, 1978\* are becoming increasingly common, it would be desirable for a definitive text to be prepared before any further conventions were adopted for which the provision would be appropriate.<sup>5</sup> Therefore, if the Commission agrees that it would be desirable to prepare such a provision for use in international conventions, the Commission may wish to adopt the provision at its next session.

7. The Commission may wish to consider requesting the Working Group on International Negotiable Instruments to prepare a draft provision to be presented to the Commission at its next session with a view to its adoption by the Commission at that time. The Commission may also wish to request the Secretary-General to conduct such studies as seem desirable in the light of the discussion in the current session of the Commission and to submit those studies to the Working Group along with a preliminary draft text.

8. In this connexion it may be noted that the Working Group on International Negotiable Instruments expects to complete the tasks currently assigned to it by the Commission at its eleventh session in August 1981.<sup>6</sup> Even if the Commission were to request the Working Group to consider the comments of Governments and interested international organizations on the draft Convention on International Bills of Exchange and International Promissory Notes and the draft Uniform Rules Applicable to International Cheques, as suggested by the Working Group,<sup>7</sup> those comments will not be received and ready for consideration until after the Commission's fifteenth session. Therefore, the Working Group, which is composed of Chile, Egypt, France, India, Nigeria, Union of Soviet Socialist Republics, United Kingdom of Great Britain and Northern Ireland and the United States of America, would be available to consider a provision on a universal unit of account in the early months of 1982.

## ANNEX I

### A unit of account for international conventions<sup>a</sup>

Increasing recognition is being accorded to use of the special drawing right (SDR) as an international unit of account. At the same time, proposals are being put forward to refine its application in international conventions. Following the adoption of the United Nations Convention on the Carriage of Goods by Sea,\* which specifies the SDR

\* Yearbook . . . 1978, part three, I, B.

<sup>2</sup> See A. Tobolewski, "The special drawing right in liability conventions: an acceptable solution?" *Uniform Law Review* (1978, II), p. 14.

<sup>3</sup> United Nations Convention on International Multimodal Transport of Goods, article 31 (TD/MR/CONF/16), adopted at Geneva on 24 May 1980; draft articles for a convention on liability and compensation in connexion with the carriage of noxious and hazardous substances by sea, article 10, IMCO document LEG XLIV/2 of 10 September 1980.

<sup>4</sup> It should be borne in mind, however, that while in principle any number of price indices might be appropriate for use in different conventions, each separate price index which might be used would require the commitment of the IMF to calculate and publish it. Therefore, it would be desirable if agreement could be reached on the use of a single price index.

\* Yearbook . . . 1978, part three, I, B.

<sup>5</sup> It is expected that the draft convention cited in footnote 3 will be submitted in 1982 to a conference of plenipotentiaries by the Intergovernmental Maritime Consultative Organization.

<sup>6</sup> Report of the Working Group on International Negotiable Instruments on the work of its tenth session, A/CN.9/196, para. 208 (reproduced in this volume, part two, II, A).

<sup>7</sup> *Ibid.*, para. 213.

<sup>a</sup> A note prepared by the IMF staff observers at the request of the UNCITRAL Secretariat.

as its unit of account, the Study Group on International Payments of the United Nations Commission on International Trade Law (UNCITRAL) began examination of a proposal made by the representative of France at the eleventh session of UNCITRAL (May 30-June 16, 1978). The proposal urged UNCITRAL to "study ways of establishing a system for determining a universal unit of constant value which would serve as a point of reference in international conventions for expressing amounts in monetary terms" (A/CN.9/156, 2 June 1978).\*

The SDR is defined as a basket of currencies containing specified amounts of the currencies of the five member countries of the International Monetary Fund (IMF) that, in a recent five-year base period (1975-79), had the largest exports of goods and services—United States, Federal Republic of Germany, Japan, France, and United Kingdom. In that base period, these five countries together accounted for almost one half of the total exports of goods and services of all IMF members. Being defined as a basket of currencies, the SDR maintains its purchasing power over the collection of component currencies as well as over any other currencies that maintain a stable relationship to the SDR. Its purchasing power over goods and services varies, however, with the purchasing power of the component currencies.

For a monetary amount specified in terms of SDRs to represent, as much as possible, a constant real value over time, the amount would have to be adjusted periodically in relation to a suitable price index. Such adjustments could be made either automatically or through a reviewing procedure. Although the latter method could in principle give some flexibility, it has the disadvantage of requiring periodic administration, which may in practice rob it of much of the flexibility it may have in principle. Moreover, the discretionary character of the method may introduce a measure of uncertainty. For these reasons an automatic procedure may recommend itself.

Under an automatic procedure, monetary amounts used in conventions would be specified in terms of an SDR with the purchasing power over goods and services actually observed in a base period. Whenever the corresponding nominal amount in terms of a particular currency is to be determined, the specified SDR amount would first be multiplied by the current value of the chosen price index before being converted into the desired currency by means of the current exchange rate between that currency and the SDR.

Two questions arise with respect to the choice of a price index: first, which of a number of available national price indices to employ and, second, the country composition of the international index. The first question does not have a general answer. The choice largely depends on the purpose of the monetary amounts to be specified. For most purposes a consumer price index would be suitable, for instance, when the amounts refer to the compensation of individuals for injuries or losses. Consumer price indices, in contrast to some other indices, are generally not subject to revision once published and are commonly used to protect contracts against the erosion of purchasing power of a national currency. It would be possible, however, to specify any of a number of other price indices—producer prices, export prices, GNP deflators, etc.—in the text of a convention if that should be found to be preferable.

As regards the country composition of the price index, it would be most logical to adapt it to the composition of the SDR itself. This would entail combining the national price indices of the countries whose currencies are contained in the SDR currency basket with weights corresponding to the currency composition of the basket. This method recommends itself for the following important reason, which has to do with the relation between prices and exchange rates. There is a tendency for differential price trends in two countries to be reflected in the exchange rate between the two currencies. This relation, although far from perfect, is too strong to be set aside in designing the

index in question. It implies that the purchasing power of an amount denominated in a particular currency can best be kept constant by correction for changes in the price index reflecting goods and services that are bought with that currency. Extension of this principle to a basket of currencies leads to the proposed index, whose composition and weighting match those of the basket.

The SDR price index can best be defined by reference to the objective that a specified amount of SDRs, multiplied by the current index value, should be just sufficient to purchase in the current period the same basket of goods and services that could have been bought with that specified amount in a chosen base period, with each of the five component currencies having been spent on a representative collection of goods and services in the respective issuing country. A formula for such an index is developed in annex II.

For strict validity, the proposed SDR price index would require constancy of both the SDR basket of currencies and the five baskets of goods and services on which the component national price indices are based. As long as these six baskets are unchanged, the SDR price index can be envisaged as a measure of the cost, expressed in SDRs, of a basket containing five national sub-baskets of goods and services. Changes in either the SDR basket or in one or several of the national consumption baskets between the base period and the current period preclude use of the index for strict comparison of the cost of a given collection of goods and services between the two periods. Nevertheless, if the changes are marginal—e.g. moderate changes in the currency composition of the SDR reflecting movements in trade shares of the five countries, or changes in the national consumption baskets as a result of alterations in consumption patterns—the index based on the new set of baskets could be linked to that based on the old set in a manner customary in the use of indices over longer time spans when weights are subject to change. Such marginal changes would not be expected to impair the general usefulness of the index as a practical measure of changes over time in the purchasing power of the SDR.

Accordingly, whenever the number of units of the five currencies in the SDR basket are altered as a result of periodic reviews of the composition of the basket, the base period should be shifted to the period (say, the month) preceding the change of the basket. The index using the new weights would be linked to that calculated with the old weights so that the index value would not jump arbitrarily as a consequence of the change in the composition of the SDR basket. Changes in the consumption baskets on which the national price indices are based are handled in a similar manner by the national statistical offices publishing them.

In the unlikely event that one of the baskets were altered more drastically—for instance, if one of the national price indices should cease to be published or if the list of currencies in the SDR basket should be changed—a new SDR price index would have to be calculated for the period following the alteration. It would then be for consideration whether monetary amounts in various conventions and agreements should be respecified in SDRs of the purchasing power attained during the base period of the new index or whether the new index should simply be linked to the old one at the period of overlap (i.e., the base period of the new index). The outcome of these two procedures would probably not differ greatly in practice, since the revision of specified monetary amounts required by the first procedure would most likely be guided by the calculated value of the old SDR price index during the period that forms the base period of the new index.

If the SDR in conjunction with a suitable SDR price index were chosen as a unit of account for use in international conventions, the data needed for calculating monthly values of the index, as well as monthly exchange rates between the SDR and the currencies of IMF member countries (and of some nonmember countries) would be available in the monthly IMF publication *International Financial Statistics*. Moreover, there would in principle appear to be no obstacle to calculation of the monthly price index by the IMF staff, with a delay of no more than three months.

\* Yearbook . . . 1978, part two, IV, C.

## ANNEX II

## Formula for an SDR price index

The SDR price index sought can be defined as the SDR amount needed at a given time,  $t$ , to purchase the basket of goods and services that could have been bought during a chosen base period with the five currency amounts of which one SDR is composed, each currency being spent on a representative collection of goods and services in the respective issuing country. The elements needed for calculating such an index are the following:

$P_{it}$  = price index of country  $i$  at time  $t$  ( $P_{i0} = 1.0$ , with period 0 being the base period);

$C_i$  = number of units of currency  $i$  in the SDR basket; and

$R_{it}$  = exchange rate of currency  $i$ , defined as the number of SDRs per unit of currency  $i$  at time  $t$ .

The product  $C_i P_{it}$  represents the number of units of currency  $i$  that are needed at time  $t$  to purchase the same basket of goods and services in country  $i$  that could have been acquired for  $C_i$  currency units in the base period.

The SDR value at time  $t$  of the collection of the five currency amounts  $C_i P_{it}$ , defined in the preceding paragraph, represents the

proposed price index for the SDR at time  $t$ . This index,  $P_{st}$ , is shown below in three alternative, though equivalent, forms:

$$P_{st} = \sum_{i=1}^5 (C_i P_{it}) R_{it} = \sum_{i=1}^5 (C_i R_{it}) P_{it} = \sum_{i=1}^5 (C_i R_{i0}) P_{it} (R_{it}/R_{i0})$$

The first of these forms (on the left) suggests the basic definition of the index, namely, the SDR value of the five currency amounts needed to purchase at time  $t$  the five national sub-baskets that could have been bought with the five currency components of the SDR in the base period.

The second formulation (in the middle) indicates that this SDR price index is the weighted average of the five component national price indices, with the current value shares of the five currencies in the SDR being used as weights.

The third formulation (on the right) suggests that the index can also be viewed as a weighted average of the national price indices measured in terms of SDRs— $P_{it}$  multiplied by  $(R_{it}/R_{i0})$ —with the base-period value shares of the five currencies in the SDR being used as weights.

If desired, the index could be multiplied by 100 in order to bring it into customary index form.

### III. INTERNATIONAL COMMERCIAL ARBITRATION\*

#### Report of the Secretary-General: possible features of a model law on international commercial arbitration (A/CN.9/207)\*\*

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#### INTRODUCTION

1. At its twelfth session, the United Nations Commission on International Trade Law considered a report of the Secretary-General entitled "Study on the application and interpretation of the Convention on the Recognition and Enforcement of Foreign Arbitral Awards (New York, 1958)" (A/CN.9/168)\*\*\* and a note by the Secretariat on further work in respect of international commercial arbitration (A/CN.9/169).\*\*\*\* The

\* For consideration by the Commission see Report, chapter IV (part one, A, above).

\*\* 14 May 1981. Referred to in Report, paras. 63, 64 (part one, A, above).

\*\*\* Yearbook . . . 1979, part two, III, C.

\*\*\*\* Yearbook . . . 1979, part two, III, D.

<sup>1</sup> Report of the United Nations Commission on International Trade Law on the work of its twelfth session, *Official Records of the General Assembly, Thirty-fourth Session, Supplement No. 17 (A/34/17)*, paras. 78-80 (Yearbook . . . 1979, part one, II, A).

note suggested that the Commission commence work on a model law on arbitral procedure which could help to overcome most of the problems identified in the above study and to reduce the legal obstacles to arbitration.

2. The Commission decided, at that session, to request the Secretary-General

"(a) To prepare an analytical compilation of provisions of national laws pertaining to arbitration procedure, including a comparison of such laws with the UNCITRAL Arbitration Rules\* and the 1958 Convention;

"(b) To prepare, in consultation with interested international organizations, in particular the Asian-African Legal Consultative Committee and the International Council for Commercial Arbitration, a

\* Yearbook . . . 1976, part one, II, A, para. 57.

preliminary draft of a model law on arbitral procedure, taking into account the conclusions reached by the Commission, and in particular:

"(i) That the scope of application of the draft uniform rules should be restricted to international commercial arbitration;

"(ii) That the draft uniform law should take into account the provisions of the 1958 Convention and of the UNCITRAL Arbitration Rules;

"(c) To submit this compilation and the draft to the Commission at a future session."<sup>2</sup>

3. At its thirteenth session, the Commission had before it a note by the Secretariat entitled "Progress report on the preparation of a model law on arbitral procedure" (A/CN.9/190).<sup>3</sup> In this note, the Secretariat set forth its initial work and referred to difficulties in obtaining the materials necessary for the preparatory work on this project. In order to assist the Secretariat in that regard, the Commission decided to invite Governments to provide the Secretariat with relevant materials on national legislation and case law, and pertinent treatises where available.<sup>4</sup> The General Assembly included a similar appeal to Governments in its resolution 35/51\* of 4 December 1980 (paragraph 12 (d)).

4. The Secretariat is indebted to those Governments which have already provided it with relevant publications. Materials of as many States and legal systems as possible are needed in order to obtain complete and current information on the different laws and legal practice in the field of arbitration. To have accurate and up-to-date information becomes particularly crucial when, at a later stage, specific issues will be discussed in detail in order to find widely acceptable solutions. Accounts of national laws on the various specific issues could then assist the Commission or, if it wishes to entrust a Working Group with that task, the Working Group in its discussions and preparation of draft provisions.

5. Before that, it seems advisable to discuss and decide on more general, preliminary issues concerning the principles, scope, and possible contents of a model law. The present report is designed to assist the Commission in its consideration of such features and the basic directions it may wish to determine.

6. The first part of the report (A) deals with the concerns which should be met by the model law and with the principles which could underlie it. Clarity and agree-

ment on these points should not only help to find the most suitable approach in this project but also help to define the scope of the future model law, in combination with the directions already decided upon by the Commission, i.e. to cover only international commercial arbitration and to take into account the provisions of the 1958 Convention and of the UNCITRAL Arbitration Rules (see decision above, paragraph 2, sub-paragraph (b) (i) and (ii)).

7. The second part of the report (B) attempts to identify all those issues possibly to be dealt with in the draft model law. It does not merely list the points commonly regulated in arbitration statutes or the relevant parts of civil procedure codes. Rather, it focuses on those issues inclusion of which would appear desirable in view of the suggested purposes and principles. In particular, it emphasizes matters where difficulties have been encountered in international practice. Thus, reference is made to problems arising out of disparities between national laws or shortcomings of legal rules or divergent attitudes in different jurisdictions, taking into account criticisms and suggestions made by practitioners and scholars. This report is not intended, though, to discuss these issues in detail and to present elaborate proposals since its purpose is merely to identify the issues and to state reasons relevant to the decision about their inclusion into the draft model law. Whether or not all the issues listed will eventually be dealt with in the model law, their discussion should provide a clearer idea about the possible scope of such a law and about the work and expertise required for its preparation.

8. It should also be mentioned here that the order and classification of the issues used in this report does in no way indicate what the eventual structure of the model law could be like. The order used in part B (except I) is simply the classification scheme of the national reports published in the *Yearbook Commercial Arbitration*.<sup>5</sup> This sensible scheme has been adopted here in order to facilitate reference to, and consultation of, these national reports with their wealth of information, on which the Secretariat relied in preparing this report.<sup>6</sup>

<sup>5</sup> Publication of the International Council for Commercial Arbitration; General Editor: Prof. Pieter Sanders; publ. by Kluwer, Postbox 23, 7400 GA Deventer, Netherlands. In the following footnotes the *Yearbook Commercial Arbitration* is referred to as "YCA".

<sup>6</sup> Reports on the laws of the following States have been published in volumes I to VI of the *Yearbook Commercial Arbitration*: Algeria, Argentina, Australia, Austria, Belgium, Brazil, Bulgaria, Canada, Chile, China, Colombia, Costa Rica, Cuba, Czechoslovakia, Denmark, Ecuador, Egypt, Finland, France, German Democratic Republic, Germany, Federal Republic of, Greece, Hungary, India, Indonesia, Iran, Iraq, Israel, Italy, Japan, Kuwait, Libyan Arab Jamahiriya, Mexico, Mongolia, Netherlands, Nigeria, Norway, Pakistan, Panama, Peru, Poland, Romania, Saudi Arabia, Sweden, Switzerland, South Africa, Union of Soviet Socialist Republics, United Kingdom of Great Britain and Northern Ireland, United States of America, Venezuela, Yugoslavia.

\* Yearbook . . . 1980, part one, II, D.

<sup>2</sup> *Ibid.*, para. 81.

<sup>3</sup> Report of the United Nations Commission on International Trade Law on the work of its thirteenth session, *Official Records of the General Assembly, Thirty-fifth Session, Supplement No. 17* (A/35/17), paras. 114-116 (Yearbook . . . 1980, part one, II, A).

<sup>4</sup> *Ibid.*, para. 117.

## A. CONCERNS AND PRINCIPLES OF A MODEL LAW ON INTERNATIONAL COMMERCIAL ARBITRATION

### 1. General concerns and problems

9. The ultimate goal of a model law would be to facilitate international commercial arbitration and to ensure its proper functioning and recognition. Its practical value would, in particular, depend on the extent to which it provides answers to the manifold problems and difficulties encountered in practice. Thus, in preparing the model law an attempt should be made to meet the concerns which have repeatedly been expressed in recent years, sometimes even labelled as "defects" or "pitfalls" in international commercial arbitration.

10. A major complaint in this respect is that the expectations of parties as expressed in their agreements on arbitration procedure are often frustrated by conflicting mandatory provisions of the applicable law. To give only a few examples, such provisions may relate to, and be deemed to unduly restrict, the freedom of the parties to submit future disputes to arbitration, or the selection and appointment of arbitrators, or the competence of the arbitral tribunal to decide on its own competence or to conduct the proceedings as deemed appropriate taking into account the parties' wishes. Other such restrictions may relate to the choice of the applicable law, both the law governing the arbitral procedure and the one applicable to the substance of the dispute. Supervision and control by courts is another important feature not always welcomed by parties especially if exerted on the merits of the case.

11. These and other restrictive factors set forth in detail below (in part B) tend to create the above disappointment with mandatory provisions of law. It is this concern which, for example, prompted the recommendation of the Asian-African Legal Consultative Committee (AALCC) as considered by the Commission at its tenth session: "Where the parties have adopted rules for the conduct of an arbitration between them, whether the rules are for *ad hoc* arbitration or for institutional arbitration, the arbitration proceedings should be conducted pursuant to those rules notwithstanding provisions to the contrary in municipal laws and the award rendered should be recognized and enforced by all Contracting States to the 1958 New York Convention".<sup>7</sup>

12. However, this suggestion should not be understood as advocating total freedom of the parties and refusal of all mandatory provisions in the field of international commercial arbitration. That is clear from the

second recommendation of the AALCC: "Where an arbitral award has been rendered under procedures which operate unfairly against either party, the recognition and enforcement of the award should be refused".<sup>8</sup> A corrective role in this regard may be played by courts in a country where recognition and enforcement of a foreign arbitral award is sought as provided for in the 1958 New York Convention. But it may also be performed by mandatory provisions of the *lex loci arbitri* dealing with defects in the procedure, denial of justice, and lack of due process of law.

13. Another source of concern and of possibly unexpected legal consequences is the non-mandatory part of the applicable law. Although, by definition, such provisions may be derogated from and, thus, the effect of any undesired rule nullified, parties may not have made a contrary stipulation, in particular where they were not aware of such rule. Also, where parties have not agreed on a certain procedural point, yet another concern may arise from the fact that the applicable law does not contain a provision settling this point. The lack of such "supplementary" rule may create uncertainty and controversy detrimental to the smooth functioning of the arbitration proceedings.

14. The above problems and undesired consequences, whether emanating from mandatory or from non-mandatory provisions or from a lack of relevant provisions, may be due to the fact that a given national law deals only with some aspects of arbitration, or that it is out-dated and in need of revision, or that it has been drafted to meet the needs of domestic arbitration, possibly emphasizing local particularities, or that for other reasons it is not adequate for modern international arbitration practice. This situation is aggravated by the fact that the applicable law often bears no substantive connexion with the parties or the dispute at hand. Usually it is the law of the place of arbitration and this, in fact, may be selected simply for reasons of convenience, for example, because it is the residence of the sole arbitrator or the chairman of a tribunal.

15. In such cases of a rather fortuitous determination of the applicable law parties may be confronted with provisions and procedures with which they are not familiar. The possible adverse effect of that is enhanced by the well-known fact that there exist wide disparities among the national laws on arbitration procedure. Even where uniformity has been achieved to a certain extent, for example, by a widely accepted multilateral convention, unexpectedly different results may be reached due to divergent interpretations of its provisions. With regard to the most important convention, this has been shown by the study on the application and interpretation of the 1958 New York Convention submitted to the Commission at its twelfth session.<sup>9</sup> In addition, there remains a

<sup>7</sup> Report of the United Nations Commission on International Trade Law on the work of its tenth session, *Official Records of the General Assembly, Thirty-second Session, Supplement No. 17 (A/32/17)*, para. 39 and annex II, paras. 27-36 (Yearbook . . . 1977, part one, II, A). The recommendation of the AALCC has been reproduced in document A/CN.9/127 (Yearbook . . . 1977, part two, III), with comments by the Secretariat in A/CN.9/127/Add.1.

<sup>8</sup> *Ibid.*

<sup>9</sup> A/CN.9/168 (Yearbook . . . 1979, part two, III, C).

great number of unsettled issues and unanswered questions (to be discussed below in part B) which might create uncertainty and controversy.

## II. General principles and purposes

16. From the general concerns expressed above some tentative conclusions may be drawn which could serve as guidelines in the preparation of a model arbitration law. It is submitted that, to minimize the indicated difficulties, the following principles and purposes should underlie the model law to be drafted.

17. Probably the most important principle on which the model law should be based is the freedom of the parties in order to facilitate the proper functioning of international commercial arbitration according to their expectations. This would allow them to freely submit their disputes to arbitration and to tailor the "rules of the game" to their specific needs. It would also enable them to take full advantage of rules and policies geared to modern international arbitration practice as, for example, embodied in the UNCITRAL Arbitration Rules.

18. To give parties the greatest possible freedom does not mean, however, to leave everything to them by not regulating it in the model law. Apart from the desirability of providing "supplementary" rules (see above, paragraph 13), what is needed is a positive confirmation or guarantee of their freedom. Thus, the model law should provide a "constitutional framework" which would recognize the parties' free will and the validity and effect of their agreements based thereon.

19. Yet, as indicated above (paragraph 12), it is not suggested to accord absolute priority to the parties' wishes over any provision of the law. Their freedom should be limited by mandatory provisions designed to prevent or to remedy certain major defects in the procedure, any instance of denial of justice or violation of due process. Such restrictions would not be contrary to the interest of the parties, at least not of the weaker and disadvantaged one in a given case. They would also meet the legitimate interest of the State concerned which could hardly be expected to issue the above guarantee without its fundamental ideas of justice being implemented.

20. Such fundamental principles as usually found in a State's *ordre public* could only be neglected if one were to favour international arbitration proceedings and awards which would be "supra-national" in the sense of a full detachment from any national law. However, the present report is based on the view that it is desirable, if not imperative, to envisage a certain link between the arbitration proceedings, including the award, and a national law which would give recognition and effect to arbitration agreements and awards and would provide for adequate assistance by courts, for example, as regards orders to compel arbitration or to call witnesses

or to enforce interim measures of protection or to provide ultimate resort in case of a deadlock. By establishing such a connexion one should also avoid the problem of a "floating" or "stateless" award which could arise where not even the courts of the State where the award was made confirm (or deny) its binding nature for lack of jurisdiction or "nationality" of the award.<sup>10</sup>

21. In view of the above, it will be one of the more delicate and complex problems of the preparation of a model law to strike a balance between the interest of the parties to freely determine the procedure to be followed and the interests of the legal system expected to give recognition and effect thereto. This involves, above all, a precise demarcation of the scope of possible intervention and supervision by courts and, in particular, of the substantive criteria for reviewing and reasons for setting aside an award. It is submitted that the result of this endeavour will have a considerable influence on the success of the whole project. Yet, the task is somewhat eased by the fact that transnational transactions tend to be subject to less strict standards than purely domestic transactions. This recent trend can be discerned, for example, from the increasingly made distinction between international public order and domestic public order of a State where recognition and enforcement of a foreign award is sought.<sup>11</sup>

22. It is, of course, not only in respect of such substantive standards for review and control that the specific characteristics of international commercial arbitration should be focused at. The needs of modern international practice and the principles of fairness and equality should be guiding in the drafting of all the provisions of a model law. Implementation of the decision of the Commission "that the draft uniform law should take into account the provisions of the 1958 Convention and of the UNCITRAL Arbitration Rules" (see above, paragraph 2) would go a long way towards meeting these ends.

23. In order to facilitate the smooth operation of international commercial arbitration, a further drafting principle could be to strive for a set of rules which would be as comprehensive and complete as possible. This would meet the above concern (paragraph 13) that lack of a provision on a certain point may create uncertainty and controversy. Completeness could also extend to matters possibly regulated in other branches of the law since their inclusion into the model law would allow to adopt uniform answers adapted to the international type of arbitration. Thus, one might even consider to include at least some of the issues not included in the otherwise fairly extensive 1966 Strasbourg Uniform Law on Arbitration: capacity to conclude an arbitration agreement,

<sup>10</sup> Cf. e.g. decision of the Cour d'Appel de Paris of 21 February 1980, 1ère Chambre civile, publ. in *Recueil Dalloz Sirey* 1980, p. 568, with a note by Robert.

<sup>11</sup> See A/CN.9/168, para. 46 (Yearbook . . . 1979, part two, III, C).



the qualifications of an arbitrator, counter-claims, the powers of investigation of an arbitral tribunal, the provisional execution of arbitral awards, arbitration costs and arbitrators' fees, the jurisdiction of judicial authorities called upon to intervene.<sup>12</sup>

24. Other issues usefully to be included are those that have given rise to difficulties due to divergent interpretations, or gaps, of the 1958 New York Convention as identified in the study of the Secretary-General (A/CN.9/168).<sup>\*</sup> Thus, clarification could be sought, for example, of the exact meaning of the requirement that the arbitration be "in writing". One could also attempt to reach agreement on the law applicable to the arbitration agreement. Another question possibly to be answered in the model law is whether pre-arbitration attachments and similar measures are compatible with an arbitration agreement. To mention yet another point of a long list of items that have given rise to difficulties, one could envisage a provision to the effect that where parties have referred to the law of a given State as being applicable to the substance of the dispute then this choice of law is deemed to refer directly to the substantive law of that State and not to the conflicts rules contained in its private international law.

25. The principle of striving for completeness should be seen in connexion with another idea which would strengthen the positive effect of assisting lawyers, arbitrators and businessmen in their difficult task to find out about the legal rules of a foreign system. And that is to envisage that the law on international commercial arbitration be accorded priority (as *lex specialis*) over other laws except as otherwise stated in the (model) arbitration law. For the same purpose, one could, for example, require the listing of certain points which are often, and for reasons of substance, regulated in other laws, e.g. any non-arbitrable subject-matters or any persons or bodies lacking the capacity to conclude arbitration agreements. This would, at least, ensure easy access to the law although it would not necessarily lead to uniformity since States may list different categories of such exclusions.

26. As to the desirable uniformity in general, it may be submitted here that a model law is not necessarily less conducive to reaching uniform standards than a convention. Apart from any considerations concerning the time-consuming and costly procedures of adopting and ratifying a convention, it is ultimately the quality of the contents of the proposed law that determines its acceptability. However, for the sake of uniformity an appeal should be envisaged to adopt the law, though a model, *in toto*. Another measure of harmonization would be to later "monitor" the interpretation and application of the law by publishing relevant court decisions and pointing

out any divergencies. That is, of course, in the true sense of the word, a *cura posterior*.

27. What has to be done first is to work towards a clear and complete set of rules establishing fair and modern standards of international arbitration which would be acceptable to the different legal and economic systems of the world. For that purpose, an attempt shall be made now to identify the issues possibly to be dealt with in the model law and to mention relevant problems and reasons.

## B. IDENTIFICATION OF ISSUES POSSIBLY TO BE DEALT WITH IN THE MODEL LAW

### I. Scope of application

28. As decided by the Commission at its twelfth session, "the scope of application of the draft uniform rules should be restricted to international commercial arbitration" (see above, paragraph 2). It seems clear that this restriction, if finally maintained, will have to be stated in the model law. It is less clear, though, whether the three elements delimiting the scope of application, i.e. "arbitration", "commercial" and "international", should be defined and, if so, in which way.

#### 1. "Arbitration"

29. As to the first element, i.e. "arbitration", it would seem desirable to define that term since it expresses the "heart of the subject-matter" or activity governed by the model law. Such definition would have to cover institutional and *ad hoc* arbitration. Also, it would in some way have to indicate that arbitration is a dispute settlement procedure outside the court system. Beyond that, however, a major difficulty will be to distinguish precisely between arbitration as regulated in the model law and those procedures which, sometimes even labelled arbitration, are similar to arbitration such as the Italian "*arbitrato irrituale*", the Dutch "*bindend advies*" and the German "*Schiedsgutachten*".

30. While certain common features of these three examples of "free arbitration" can be detected (e.g. determination of questions of fact rather than law and decision merely binding like a contract provision), these procedures are not identical and there are yet other such procedures in other legal systems. Thus, it will not be an easy task to draw the line in a sufficiently clear manner. At the very least, one should envisage an appeal to States adopting the model law to list any procedure akin to arbitration but excluded from its scope of application.

#### 2. "Commercial"

31. As to the second element delimiting the scope of application, i.e. "commercial", it is doubtful whether that should be defined in the model law. It may be

<sup>\*</sup> Yearbook . . . 1979, part two, III, C.

<sup>12</sup> See General Considerations, para. 7, of the Explanatory Report on the European Convention Providing a Uniform Law on Arbitration, Council of Europe, 1967.

thought that this term, although not always and in all respects construed in an identical manner, has by now gained a sufficiently clear meaning, at least as a modifier to arbitration, thus excluding arbitrations of a different nature such as those in labour disputes or family law matters. Based on the experience with article I, paragraph 13 of the 1958 New York Convention,<sup>13</sup> it is further suggested not to qualify the term along the following lines: "relationships which are considered as commercial under the national law of the respective State".

### 3. "International"

32. As to the third element, i.e. "international", it would seem necessary, though difficult, to define that term since the model law is designed to provide a special legal regime for those arbitrations where more than purely domestic interests are involved. There are a number of possible criteria to regard an arbitration as "international" in the sense of "not purely domestic". One such instance would be that at least one of the parties has its place of business in, or is a national of, a State other than the one concerned (hereinafter called X). Another factor could be that the place of arbitration lies outside State X. Yet other factors may be that the arbitration agreement (or the contract containing the arbitration clause) is concluded in a State other than X or that the subject-matter of the dispute concerns an area outside State X (e.g. the market regulated in a distribution agreement.).

33. The first two criteria are used, for example, in the United Kingdom Arbitration Act 1979 which defines, in section 3(7),

"domestic arbitration agreement" as an "arbitration agreement which does not provide, expressly or by implication, for arbitration in a State other than the United Kingdom and to which neither

"(a) An individual who is a national of, or habitually resident in, any State other than the United Kingdom, nor

"(b) A body corporate which is incorporated in, or whose central management and control is exercised in, any State other than the United Kingdom,

"is a party at the time the arbitration agreement is entered into".

It has been observed that, in this definition, the ambit of a non-domestic arbitration is drawn very widely in order to give essentially international arbitrations the full benefit of the relaxation introduced by the new legislation.<sup>14</sup> In view of this international thrust and of the technique employed (i.e. to define domestic rather than

non-domestic), the above definition may seem to commend itself as an interesting model.

34. However, for the purposes of the scope of application of the model law which is to cover various stages of arbitration (e.g. conclusion of arbitration agreement, arbitral proceedings, setting aside of award, recognition and enforcement of award), certain difficulties should not be overlooked which may arise, in particular, when the place of arbitration is used as a distinguishing factor. One difficulty relates to the fact that the question of the applicability of the model law, based on the non-domestic character of the arbitration, may already be relevant before the arbitration has started, e.g. in the context of a referral to arbitration as envisaged under article II, paragraph 3 of the 1958 New York Convention. Uncertainty would then exist if, as is sometimes the case, the arbitration agreement does not specify the place of arbitration but leaves that determination to the arbitrator. Such an arbitration agreement, if concluded between two nationals of State X, would under the above definition conceivably be treated as a domestic one since it "does not provide for arbitration in a State other than X". If a foreign party is involved, then this would be the international connexion bringing it within the scope of the model law. Consequently, one might consider to solely rely on this criterion, i.e. foreign place of business or nationality of at least one of the parties.

35. This suggestion could also meet the following concern: A State (X) may not be willing to apply its "relaxed" international arbitration provisions to the situation where, as would be covered under the above definition, two nationals of that State select a foreign place of arbitration (and could, thus, avoid the more restrictive procedural law for domestic cases). On the other hand, the State where the arbitration takes place may have no objection against the application of its "international" arbitration law even if both parties are from the same foreign country. The same may be true where in this State a stay of proceedings is sought based on such an arbitration agreement.

36. There is yet another concern in respect of those provisions of the model law which would govern the arbitration proceedings and any setting aside procedures. One should expect that these provisions would primarily, though not exclusively, apply to those "international" arbitrations which take place within the boundaries of the State concerned (X). This expectation is based on the existing conflicts rules according to which the applicable procedural law is normally the law of the place of arbitration, except where another law is validly chosen by the parties. Although the above definition could technically work here since it would not prevent the application of the law to arbitrations in State X as long as at least one of the parties is a national of another State, the use of the (foreign) place of arbitration as one

<sup>13</sup> Cf. A/CN.9/168, para. 11 (Yearbook . . . 1979, part two, III, C).

<sup>14</sup> Schmitthoff, *The United Kingdom Arbitration Act 1979*, YCA V-1980, pp. 231, 234.

of two alternative criteria could be regarded as misleading or as a matter of misplaced emphasis. In fact, the place of business (or nationality) of the parties remains as the decisive factor.

37. If, thus, one were to require that the parties are from different States, one would certainly exclude purely domestic arbitrations. This would also include cases where none of the parties is from the State concerned. Yet, it may be doubtful whether the law of State X should apply to such "fully non-domestic" cases since one might assume that a certain connexion with that State should exist. Here, one may well take the position that this is not an issue to be dealt with under "scope of application", the purpose of which is to indicate generally what type of cases the law is designed to regulate.

38. The above examples, to which many could be added, indicate not only the complexity of the issue at hand but also the inter-play or interdependence between the scope of application and the pertinent conflicts rules. Therefore, the Commission may wish to discuss to what extent such considerations should be taken into account when defining the scope of application and it may even wish to decide whether it would not be appropriate to envisage inclusion of some model conflicts rules. Whatever the final answer may be, the relevant provisions of the 1958 New York Convention would have to be taken into account in order to avoid any conflict and, at least with regard to the scope of application, an attempt should be made to use the same criterion or criteria for the various stages of arbitration regulated by the model law.

## II. Arbitration agreement

39. In contrast to court litigation, arbitration proceedings usually take place only if the parties have so agreed. Therefore, the model law should contain provisions on this basic agreement. It should be mentioned, however, that there are exceptions to this rule where no such agreement is needed since submission to arbitration is by operation of a law. The most prominent example are disputes between enterprises of the member States of the Council for Mutual Economic Assistance which, under the 1972 Moscow Convention or the General Conditions of Delivery of Goods, 1968 (sections 90 and 91), are referred to the arbitration courts attached to the Chambers of Foreign Trade, Commerce or Industry. For the sake of complete information, one might consider to envisage in the model law inclusion of a reference to the respective exceptions in a given legal system.

40. Returning now to the cases where an agreement is needed, the discussion of what constitutes an arbitration agreement, what form and contents should be required, and of other related points to be dealt with in the model law should be based on the pertinent provisions of the 1958 New York Convention:

### "Article II

"1. Each Contracting State shall recognize an agreement in writing under which the parties undertake to submit to arbitration all or any differences which have arisen or which may arise between them in respect of a defined legal relationship, whether contractual or not, concerning a subject-matter capable of settlement by arbitration.

"2. The term 'agreement in writing' shall include an arbitral clause in a contract or an arbitration agreement, signed by the parties or contained in an exchange of letters or telegrams.

### "Article V

"1. Recognition and enforcement of the award may be refused, at the request of the party against whom it is invoked, only if that party furnishes to the competent authority where the recognition and enforcement is sought proof that:

"(a) the parties to the agreement referred to in article II were, under the law applicable to them, under some incapacity, or the said agreement is not valid under the law to which the parties have subjected it or, failing any indication thereon, under the law of the country where the award was made; . . ."

For the sake of consistency between major legal texts governing international arbitration practice, it would be desirable not to include provisions in the model law which would be in conflict with any of the above rules.

#### 1. Form, validity and contents

41. It may be considered to adopt in the model law the requirement that the arbitration agreement be in writing, as envisaged under article II, paragraph 1 of the 1958 New York Convention. A survey of national laws reveals that this is the form required under most legal systems. Where this is not so, it has been reported that, nevertheless, in practice almost all agreements are concluded in writing or that oral agreements may not easily be relied on due to strict standards of proof. In some other (Latin American) States written form is dispensed with only for an agreement to arbitrate future disputes which, however, is of lesser practical value since at any rate a formal submission is required there once the dispute has arisen.

42. In view of this latter situation, it may be suggested here already that the model law not retain the classic distinction between "*compromis*" and "*clause compromissoire*". Rather, in conformity with modern arbitration principles, an arbitration agreement could relate to existing or to future disputes, as envisaged under article II, paragraph 1 of the 1958 New York Convention. Such undertaking, whether in an arbitral clause or a separate agreement, constitutes a final and sufficient

commitment by the parties. No additional submission would be necessary and, thus, its often strict formalities (e.g. public deed, recording in court) would no longer have to be observed. In view of the relaxation under the systems affected, the above proposal as to written form could be regarded as an acceptable compromise.

43. If the requirement of written form were to be adopted, it may further be suggested to include in the model law a clear and detailed definition of what "in writing" means. Such definition could help to achieve uniform interpretation which would be highly desirable not only for purposes of the model law itself but also for other legal texts such as the 1958 New York Convention (article II) or the United Nations Convention on the Carriage of Goods by Sea, 1978 (article 22).<sup>\*</sup> One might even consider to state expressly in the model law that the definition given there would be applicable to relevant provisions in other legal texts, too. As to the possible shape of such a definition, it may be based on the definition set forth in the 1958 New York Convention (article II, paragraph 2). However, in view of the difficulties encountered in practice, as reported in the study of the Secretary-General (A/CN.9/168, paragraphs 19-26), the definition in the model law should be more precise and detailed. In particular, it should attempt to tackle these problems which relate, for example, to the involvement of intermediaries, to the commercial practice of sales confirmations, or to the use of standard forms or references to general conditions.

44. Turning to the matter of validity of the arbitration agreement, it seems doubtful whether the model law should attempt to provide an exhaustive list of reasons of invalidity. Probably the best approach would be to include only those reasons which relate directly to arbitration and to leave out the other reasons relevant to any agreement or contract (e.g. mistake). An example of the first type is provided in article 3 of the Strasbourg Uniform Law: "An arbitration agreement shall not be valid if it gives one of the parties thereto a privileged position with regard to the appointment of the arbitrator or arbitrators".

45. The less matters of validity are regulated in the model law, the greater would be the need for a provision determining the law applicable to the validity of the arbitration agreement. The rule of the 1958 New York Convention (article V, paragraph 1 (a)) cannot simply be adopted. Its first alternative ("the law to which the parties have subjected it") creates difficulties where the parties' freedom of choosing a law is limited and, more importantly, the supplementary alternative ("the law of the country where the award was made") is not sufficient since, as pointed out earlier (paragraph 33), the issue may be relevant already at a time when the place of the arbitration or the award is not yet determined. Thus,

additional criteria (e.g. place of conclusion of agreement, law governing substance of dispute) would have to be considered if one were to tackle this controversial issue at all in the model law.

46. A related question is what the arbitration agreement should contain. As pointed out earlier (paragraph 40), the undertaking to submit to arbitration may relate to existing or to future disputes. It will have to be considered whether the type of dispute should be more specifically described and whether any other requirements as to the minimum contents of an arbitration agreement should be included in the model law. For example, article II, paragraph 1 of the 1958 New York Convention refers to differences "in respect of a defined legal relationship, whether contractual or not, concerning a subject matter capable of settlement by arbitration".

47. Accordingly, one may also in the model law require that the parties specify the relevant contract or other relationship. On the other hand, the restriction as to arbitrability of the subject matter need not be expressed in the arbitration agreement. However, one should state this limitation in the model law, possibly together with a listing of non-arbitrable subject matters, i.e. exclusions from the domain of arbitration dealt with below (paragraphs 55-56). Another requirement found in some national laws would be that the agreement already name the arbitrator(s) or at least set forth the appointment procedure. While parties may be recommended to do so, a strict requirement to that effect does not seem to be warranted. In this context, mention should be made of a later suggestion that the model law provide supplementary rules on the appointment procedure for cases where such procedure has not been agreed upon by the parties or does not operate as expected (below, paragraph 69).

## 2. *Parties to the agreement*

48. In order to provide wide access to arbitration, in accordance with a clearly discernible trend in modern dispute settlement practice, an attempt should be made to allow all (physical or legal) persons to conclude an arbitration agreement. The idea of envisaging no restrictions in that regard relates, of course, only to the specific capacity to submit to arbitration but not to the general capacity to conclude agreements (as, e.g. restricted for minors). Also, it is not intended to prevent, for example, a trade association from providing access to its arbitration facilities exclusively to its members. What is intended, is merely that no category of persons or corporations or organs would be *per se* excluded by law.

49. The attempt to abolish any existing restrictions in order to grant full access to arbitration may prove to be difficult with regard to governmental agencies or similar entities of public law since important State interests are

<sup>\*</sup> Yearbook . . . 1978, part three, I, B.

at stake here, including the competence of internal organization and division of authority. Nevertheless, the difficulties could possibly be overcome in view of the specific field of application, i.e. international commercial arbitration. As to the commercial aspect of the transactions concerned, a liberal rule on the capacity to arbitrate may be less objectionable since arbitration is a common procedure of dispute settlement in this field and this type of activity is not closely connected with the State's interest in shaping its policy and conducting its public affairs as it wishes. As to the international aspect, a State may adopt a more liberal attitude with regard to international transactions and disputes than to purely domestic affairs; such a distinction is, for example, clearly drawn in France.<sup>15</sup>

50. In view of the above, one might consider adopting a rule along the lines of article II(1) of the 1961 European Convention on International Commercial Arbitration according to which "legal persons considered by the law which is applicable to them as 'legal persons of public law' have the right to conclude valid arbitration agreements". Paragraph 2 of that article permits a Contracting State "to declare that it limits the above faculty to such conditions as may be stated in its declaration". One could envisage to include in the model law a similar "reservation" by requesting States to list any exclusions if such exclusions are deemed necessary.

51. In this context of State participation in arbitration, the Commission may wish to consider whether the model law should deal with pertinent aspects of State immunity. It may be recalled that one of the recommendations of the AALCC, considered by the Commission at its tenth session,<sup>16</sup> was the following point: "Where a governmental agency is a party to a commercial transaction in which it has entered into an arbitration agreement, it should not be able to invoke sovereign immunity in respect of an arbitration pursuant to that agreement".<sup>17</sup> As specified by the Sub-Committee on Trade Law of the AALCC, the intention of that proposal is to prevent a governmental agency which had entered into a valid arbitration agreement in a commercial transaction from invoking sovereign immunity, at all stages of arbitration, including the stage of recognition and enforcement of the arbitral award.<sup>18</sup>

52. It may be thought that the issue of sovereign immunity in the context of arbitration is but a part of a more general and complex problem having an obviously

political and public international law character.<sup>19</sup> Nevertheless, it is suggested not to exclude the issue without prior discussion from the preparatory work on the model law. It may even be possible to find an acceptable solution in view of the fact that it would be limited to commercial activities of States and its organs which are widely perceived, as reflected in most laws,<sup>20</sup> not as an exercise of sovereign power warranting special privileges ("*acta jure imperii*") but as being on equal footing with the activities of private corporations or persons ("*acta jure gestionis*").

53. Another encouraging consideration could be that, since arbitration depends on a commitment to arbitrate, any restrictions as to sovereign immunity would apply in practice only if a governmental agency concludes an arbitration agreement. If, in fact, a governmental agency or similar body chooses to enter into an arbitration agreement, it would seem to be appropriate that it honour its commitment to the other party reasonably relying thereon.

54. Therefore, thought may be given to including in the model law a provision on some kind of waiver of the plea or defence of sovereign immunity, either an implied waiver or, at least, a recommendation to expressly agree not to invoke sovereign immunity. In either case, one would have to study in detail the feasibility and the legal effects of such approach, both with regard to the arbitration proceedings proper, including jurisdiction of the courts to whose control the arbitration is subject, and to the recognition and enforcement of the award.

### 3. Domain of arbitration

55. Most legal systems exclude from the domain of arbitration one or more subject matters, often by establishing exclusive jurisdiction of certain courts. Commercial subject matters of this kind relate, for example, to bankruptcy, anti-trust, securities, patents, trademarks and copyrights. However, as the survey of court decisions on the 1958 New York Convention revealed,<sup>21</sup> restrictive national laws are increasingly applied in a more lenient way to international transactions than to purely domestic ones or even interpreted as merely governing domestic affairs.

56. It would be in line with this trend and beneficial to the practice of international commercial arbitration if an attempt were made to limit, to the extent possible, the number of non-arbitrable subject matters. As to the subject matters exclusion of which appears necessary, e.g. concerning customs or foreign exchange control

<sup>15</sup> The Supreme Court decided, on 2 May 1966, that Article 2060 Code Civil, according to which neither the State nor public entities may enter into an arbitration agreement, does not apply to international contracts (Cass. Civ. I, Dalloz 1966, 575).

<sup>16</sup> Report of the United Nations Commission on International Trade Law on the work of its tenth session, *Official Records of the General Assembly, Thirty-second Session, Supplement No. 17 (A/32/17)*, annex II, paras. 27-37 (Yearbook . . . 1977, part one, II, A).

<sup>17</sup> A/CN.9/127, annex, under 3(c) (Yearbook . . . 1977, part two, III).

<sup>18</sup> A/CN.9/127/Add.1, paras. 11, 12.

<sup>19</sup> Cf. reservations expressed with regard to States and Governments during discussions at the Commission's tenth session, *ibid.* (footnote 16), para. 33.

<sup>20</sup> Cf. e.g. collection of articles on various national systems in 10 *Neth. Yearb. Int. Law* 1979, p. 3 *et seq.*

<sup>21</sup> A/CN.9/168, para. 45 (Yearbook . . . 1979, part two, III, C).

regulations, one could envisage to request their listing by each State adopting the model law. This would provide easy reference and certainty about that point and, thus, be of assistance to foreign lawyers and businessmen.

57. Another question to be considered in the context of arbitrability is whether arbitration of a dispute relating to a contract may extend to what is often called "filling of gaps". When discussing this controversial issue, a distinction should be drawn between the true filling of gaps, i.e. of points that the parties intended to cover in their agreement but did not do so, intentionally or not, and the adaptation of contracts due to changed circumstances, which were unforeseeable and, thus, could not have been contemplated by the parties when concluding the agreement. It will have to be discussed separately for each of these functions whether arbitrators may perform that task without prior authorization by the parties and, if not, whether there should be any limits to the legal effects of a prior authorization.

#### 4. Separability of arbitral clause

58. It is suggested that the model law take a clear stand in favour of separability or autonomy of the arbitration clause, as adopted in modern arbitration laws and rules.<sup>22</sup> This means that an arbitration clause which forms part of a contract shall be treated as an agreement independent of the other terms of the contract. This independence may become relevant to, and facilitate, a ruling of the arbitral tribunal on objections that it has no jurisdiction, where those objections relate to the existence or validity of the arbitration clause. Another useful import of separability is that a decision by the arbitral tribunal that the contract is null and void would not entail *ipso jure* the invalidity of the arbitration clause.

#### 5. Effect of the agreement

59. The purpose of an arbitration agreement is to settle any dispute by arbitration, to the exclusion of normal court jurisdiction. If one of the parties nevertheless submits a claim concerning the matter in dispute to a court, the other party should be able to successfully invoke the arbitration agreement. The question then is whether the court should have any discretion and what points it should examine in deciding whether the parties should be referred to arbitration. Article II(3) of the 1958 New York Convention provides the following answer:

"The court of a Contracting State, when seized of an action in a matter in respect of which the parties have made an agreement within the meaning of this article, shall,\* at the request of one of the parties, refer the

parties to arbitration, unless it finds that the said agreement is null and void, inoperative or incapable of being performed."

60. It is submitted that the substance of this provision, for the sake of conformity, should be adopted in the model law. However, some supplementary provisions, not in conflict with it, may help to clarify matters. For example, one could attempt to specify the type of the court decision referring parties to arbitration, e.g. stay or dismissal of court proceedings. In this context, one could also consider providing for an order to compel arbitration. Another issue in need of clarification, as the survey of court decisions revealed,<sup>23</sup> is the complex situation, not uncommon in international commerce, where more than two parties are involved, not all of whom are bound by arbitration agreements. Another issue possibly to be dealt with is up to what stage of the court proceedings a party may successfully invoke the arbitration agreement.

61. Yet another clarification relates to the scope of application dealt with at another place (above, paragraphs 31-38). The value of a clear provision on this point becomes apparent if one considers the difficulties and disparities caused by the lack of such a provision in the 1958 New York Convention.<sup>24</sup> Finally, the model law may provide an answer to the question whether attachments or similar court measures of protection are compatible with an arbitration agreement. Again, the lack of a pertinent provision in the 1958 New York Convention has led to divergent court decisions.<sup>25</sup> A provision, supposedly in favour of compatibility, could be included here since it concerns also the pre-arbitration stage or it may be combined with the provisions governing the arbitration proceedings (below, paragraphs 77 and 78).

#### 6. Termination

62. It may be considered to specify in the model law certain circumstances under which an arbitration agreement would be terminated or would not be terminated. Examples, not necessarily to be followed, are provided by the 1966 Strasbourg Uniform Law. According to article 10(1), the arbitration agreement shall terminate *ipso jure*, if an arbitrator who has been named in the agreement dies, or cannot for a reason of law or of fact perform his office, or refuses to accept it, or does not carry it out, or if his office is terminated by mutual agreement of the parties. Article 19 regulates the period of time within which the award is to be made and then provides, in paragraph 4, that "where arbitrators are named in the arbitration agreement and the award is not made within the relevant period, the arbitration agree-

\* It may be noted that the word "shall" was erroneously omitted in the first official publication of the Convention, in United Nations, Treaty Series, vol. 330, No. 4739 (1959), pp. 38, 40, and is, consequently, missing in a number of reproductions based on that text.

<sup>22</sup> Cf. e.g. article 21, UNCITRAL Arbitration Rules (Yearbook . . . 1976, part one, II, A, para. 57).

<sup>23</sup> A/CN.9/168, paras. 27-28 (Yearbook . . . 1979, part two, III, C).

<sup>24</sup> Cf. A/CN.9/168, paras. 16-18 (Yearbook . . . 1979, part two, III, C).

<sup>25</sup> A/CN.9/168, para. 29 (Yearbook . . . 1979, part two, III, C).



ment shall terminate *ipso jure*, unless the parties have agreed otherwise". An example of non-termination is provided by article 11: "Unless the parties have agreed otherwise, neither the arbitration agreement nor the office of arbitrator shall be terminated by the death of one of the parties".

63. Another detailed question possibly to be dealt with is whether an arbitration agreement is terminated by a settlement on agreed terms ("*accord des parties*"), whereby a distinction may be drawn between agreed settlements in the form of an award and those in the form of a normal agreement.

### III. Arbitrators

#### 1. Qualifications

64. It seems doubtful whether the model law should contain any provisions on who may act as an arbitrator. It would be difficult to list certain required qualifications except very general ones which would be of minimal practical value. It would also be difficult to agree on whether any specific category of persons should be ineligible (e.g. judges); one should be able to agree, though, that foreigners should not be excluded.<sup>26</sup> If any rule on eligibility or qualifications were envisaged at all, it should indicate to what extent any restriction expressed therein would prevail over any conflicting provision in the individual arbitration agreement or the applicable standard rules of arbitration institutions or trade associations.

#### 2. Challenge

65. As regards challenge of arbitrators, the issues to be considered are on what grounds an arbitrator may be challenged and by what procedure, including any court involvement. National laws often list in detail the grounds for challenge, usually the same as apply to judges. The reasons relate to the dispute at hand such as a financial interest or previous involvement in the subject-matter under dispute or a certain relation to one of the parties. It will have to be seen whether a "uniform" list of reasons could be agreed on or whether one should merely include a general formula such as "circumstances giving rise to justifiable doubts as to the arbitrator's impartiality or independence".

66. As to the procedure of challenging an arbitrator, it is suggested that the model law guarantee the parties' freedom to agree on the procedure to be followed in case of a challenge. In particular, it should recognize any agreement as to the person or body called upon to decide about the challenge (e.g. the arbitral tribunal, the Court

of Arbitration, the Secretary or a special committee of an arbitration association, or an appointing authority). However, it will have to be considered, and expressly stated in the model law, whether resort to courts should be allowed only if so stipulated in the arbitration agreement or whether it should be envisaged, irrespective of such stipulation, as a last resort in order to avoid a deadlock. Finally, one may consider providing "supplementary" rules for those cases where parties have not regulated the challenge procedure. One might add ancillary rules on disclosure and restrictions to the right to challenge along the lines of articles 9 and 10 (2) of the UNCITRAL Arbitration Rules<sup>27</sup> and article 12 (2) of the 1966 Strasbourg Uniform Law.<sup>28</sup>

#### 3. Number of arbitrators

67. The number of arbitrators may be thought to be one of the issues that should be fully left to the parties' discretion and agreement. However, one might consider requiring an uneven number as, for example, envisaged by article 5 (1) and (2) of the 1966 Strasbourg Uniform Law.<sup>29</sup> Yet, while such requirement could enhance the efficiency of arbitration, it may be deemed as an over-protective legislative measure. As to the special feature, known in some systems, of a third arbitrator acting as an "umpire" or as a "referee", it is suggested that the model law recognize such function if envisaged in an arbitration agreement but not include it in any "supplementary" rules. As a "supplement", one might consider providing for arbitration by three arbitrators if the parties have failed to agree on a number.

#### 4. Appointment of arbitrators (and replacement)

68. The model law should guarantee the parties' freedom to agree on the appointment procedure, provided that equality is ensured (cf. above, paragraph 43). This would include the common system of party-arbitration, under which each party is to appoint one arbitrator and these two party-appointees then appoint the third arbitrator.

69. One may also consider establishing in "supplementary rules" a "reserve" mechanism for those cases where parties have not agreed on the appointment pro-

<sup>27</sup> Article 9: "A prospective arbitrator shall disclose to those who approach him in connexion with his possible appointment any circumstances likely to give rise to justifiable doubts as to his impartiality or independence. An arbitrator, once appointed or chosen, shall disclose such circumstances to the parties unless they have already been informed by him of these circumstances."

Article 10 (2): "A party may challenge the arbitrator appointed by him only for reasons of which he becomes aware after the appointment has been made."

<sup>28</sup> Article 12 (2): "A party may not challenge an arbitrator appointed by him except on a ground of which the party becomes aware after the appointment."

<sup>29</sup> Article 5: "1. The arbitral tribunal shall be composed of an uneven number of arbitrators. There may be a sole arbitrator.

"2. If the arbitration agreement provides for an even number of arbitrators, an additional arbitrator shall be appointed."

<sup>26</sup> Cf. e.g. article 2 of the 1966 Strasbourg Convention: "Each Contracting Party undertakes not to maintain or introduce into its law provisions excluding aliens from being arbitrators".



cedure, or where a party fails to appoint his arbitrator or where two arbitrators fail to appoint the third if so required under the agreed scheme. Here, one may discuss to what extent and under what conditions resort to courts may be had in such "defective" cases. In addition, some provisions may be in place concerning the reasons and procedures for replacement of an arbitrator.

#### 5. *Liability*

70. The question to what extent an arbitrator may be liable for any misconduct or error is often debated these days. National laws if they deal with this issue at all tend to apply the same (lenient) standards as adopted for judges. In view of the fact that the liability problem is not widely regulated and remains highly controversial, it may seem doubtful whether the model law could provide a satisfactory solution. However, the Commission may wish to consider in this context whether it would not be desirable to initiate the preparation of a code of conduct, or code of ethics which, outside the model law, could provide guidance to arbitrators in performing their important functions.

### IV. *Arbitral procedure*

#### 1. *Place of arbitration*

71. The model law should recognize the parties' freedom to determine the place of arbitration except where that freedom is restricted by a mandatory provision such as article 22 of the Hamburg Rules. For those cases where parties have neither determined the place of arbitration nor entrusted a third person or body (e.g. arbitral tribunal, secretariat of arbitral institution) with that decision the model law might empower the arbitral tribunal to determine the place of the arbitration.

72. "Place of arbitration" would not necessarily mean that, in fact, all meetings or hearings are held at that place (cf. e.g. article 16(2) and (3) of the UNCITRAL Arbitration Rules) but its clear determination is of legal importance in various respects. The award shall be made at that place and, as often required by national laws, filed or registered there within a certain time-period. Above all, the place of arbitration where the award was made is the major criterion to determine the applicability of the 1958 New York Convention as regards recognition and enforcement of awards (article I(1)). Yet another legal consequence arises from the not uncommon fact that the parties' choice of the place of arbitration is interpreted as implying a choice of the applicable procedural law if there is no express stipulation on that point. It may be considered to deal with this interpretation which is controversial and not beyond all doubts, if conflicts aspects were to be addressed at all in the model law (cf. above, paragraph 38).

#### 2. *Arbitral proceedings in general*

73. The model law should empower the arbitral tribunal to conduct the arbitration proceedings in such manner as it considers appropriate, subject to the following restrictions. The arbitral tribunal must treat the parties with equality and give each party at any stage of the proceedings a full opportunity of presenting his case. It should also follow any procedural instructions which the parties may have given specifically or by reference to a set of arbitration rules.

74. Furthermore, the model law may impose certain rules which would be binding on the arbitrators either irrespective of any conflicting agreement by the parties or only if the parties have not agreed otherwise. Examples of the first category, i.e. mandatory rules, include provisions on interim measures of protection by courts (discussed below, paragraph 78), on default of a party (paragraphs 80-81), and on pleas as to the jurisdiction of arbitrators, which are discussed in the section on awards since they are often dealt with in the award (paragraphs 88-89). Examples of the second category, i.e. rules from which the parties may derogate, include provisions on evidence (paragraph 75), on experts (paragraph 76), and on representation and assistance (paragraph 79). One might add provisions on hearings, on amendments to claim or defence, or on the language(s) to be used in the proceedings, whereby the language of the arbitration agreement might be considered as a possible determinant.

#### 3. *Evidence*

75. Subject to any rules agreed upon by the parties, the arbitral tribunal should be free, under the model law, to adopt and follow its own rules on evidence, including the right to determine the admissibility, relevance and weight of any evidence offered. Since the arbitral tribunal lacks the power of enforcing its procedural decisions such as calling a witness or requiring production of a document by a party, the model law may envisage some assistance by courts in that regard. Here, one would have to clearly define the possible court measures and their specific conditions. In addition, the model law could contain "supplementary" rules (e.g. along the lines of articles 24 and 25 of the UNCITRAL Arbitration Rules) for those cases where the parties have not agreed on rules on evidence.

#### 4. *Experts*

76. As regards rules on the use of experts in arbitration proceedings, similar considerations apply as on evidence in general. Thus, subject to any agreement by the parties, the arbitral tribunal would have the power to appoint experts, whereby the model law should specify whether it may do so only upon request by a party or *ex officio*. Supplementary rules could prove to be particu-

larly useful here, since a number of important questions are not normally taken into account by the parties when drawing up the arbitration agreement and are regulated in full detail only in few standard arbitration rules. Therefore, it would seem desirable to include supplementary provisions, modelled after article 27 of the UNCITRAL Arbitration Rules, on such points as the expert's terms of reference and the parties' rights and obligations in respect of the expert's performance of his task.

#### 5. *Interim measures of protection*

77. It is suggested that the model law contain provisions on interim measures such as ordering the deposit of goods with a third person or the sale of perishable goods or attachments or seizures of assets. One issue to be settled is whether the arbitral tribunal may take such measures even without being specifically empowered to do so by the parties. Then it should be determined what types of measures would be included and whether any executory assistance by courts should be provided for.

78. A court may be involved not only by lending its executory force to measures taken by the arbitral tribunal but also by taking itself such decision in the first place if so requested by a party. It may be considered whether such court measures and their conditions could be regulated in the model law or whether these issues should better be left to the general law on procedure. In either case, however, it would seem desirable to answer, probably in the affirmative, the question whether a request for such interim measures is compatible with the arbitration agreement and does not constitute a waiver thereof. As mentioned earlier (above, paragraph 61), this question may become relevant already before the commencement of arbitration proceedings.

#### 6. *Representation and assistance*

79. Questions relating to representation and assistance are, for example, whether and by what persons a party may be represented or assisted, whether the arbitral tribunal may require a party to appear in person, and whether advance notice has to be given about the persons representing or assisting a party. While a number of national laws (and the 1966 Strasbourg Uniform Law, in article 16 (4)) contain provisions on this point, it may be doubted whether there is a real need for dealing with this topic in the model law.

#### 7. *Default*

80. The model law should regulate the consequences of default of a party, at least as regards the respondent/defendant. In order to provide arbitration with its necessary "teeth", the arbitral tribunal may be empowered to continue with the proceedings and make a binding award even if the respondent fails to participate

without showing sufficient cause therefor. However, such a potentially harsh measure would seem justified only if certain conditions, based on the principles of due process and justice, are met which the model law should set forth in detail.

81. First, the party in default must have been duly notified in advance. A second requirement is that the arbitration tribunal clearly establish its competence. For that, it has to determine the existence of a valid arbitration agreement which may not be an easy task in case of silence of the respondent. The third restriction relates to the substance of the dispute and the decision about it. The arbitral tribunal may not accept without proper investigation, including the taking of evidence, the reasons and explanations given by the claimant in support of his claim. It will be necessary to exactly define this requirement of investigation which is contrary to most procedural laws on default in court litigation.

### V. *Award*

#### 1. *Types of awards*

82. It seems doubtful whether there is a real need for the model law to deal with the different possible types of awards. If it were considered to include this item, the arbitral tribunal should, in addition to making a final award, be entitled to make interim, interlocutory, or partial awards and ought to do so, if jointly requested by the parties.

#### 2. *Making of award*

83. There are essentially two procedural issues to be considered relating to the making of the award. One is the period of time within which the award shall be made, the other one is the process of making the decision to be embodied in the award.

84. The idea of establishing a time-period, as done in some national laws, might be regarded as a good one since it could help to prevent delays but regulating it in an appropriate manner will not be an easy task. One difficulty is that a fixed standard period would not be appropriate in all cases which in turn would necessitate an elaborate mechanism for extensions. Further formalities, not necessarily conducive to speedy proceedings, would be added if one were to envisage fixing of the time-period by a court (thus, e.g. article 19 (2) of the 1966 Strasbourg Uniform Law).<sup>30</sup> Additional problems may arise from the possible sanction for non-compliance which could be termination of the mandate of the arbitral tribunal.

<sup>30</sup> Article 19 (2): "If the parties have not prescribed a period or a method of prescribing a period, if the arbitral tribunal delays in making the award and if a period of six months has elapsed from the date on which all the arbitrators accepted office in respect of the dispute submitted to arbitration, the judicial authority may, at the request of one of the parties, stipulate a period for the arbitral tribunal."

trator(s).<sup>31</sup> In view of these difficulties, one might well consider to leave this issue fully to the parties who may take care of it by establishing a time-period and a procedure tailored to their needs or by selecting efficient arbitrators in the first place.

85. As to the decision-making process in arbitration proceedings with more than one arbitrator, the basic question will be whether the model law should impose certain standards or whether it should leave that issue to the parties and only establish "supplementary" rules, if deemed desirable. In view of the legal status of an award in terms of its recognition and enforceability, a mandatory rule may seem preferable. It could require that the award be made by a majority of the arbitrators; yet, in the exceptional case that a majority cannot be obtained, the model law may recognize an agreement by the parties to the effect that the chairman shall have a casting vote. For the sake of clarification, one might add that all arbitrators have to take part in the deliberations leading to the award.

### 3. Form of award

86. An obvious requirement as to the form of the award is that it be in writing. Another obvious requirement, equally common in national laws, is that it be signed by the arbitrator(s). However, national laws differ on whether any exceptions should be allowed here in the case of arbitration proceedings with more than one arbitrator. Probably the most acceptable compromise in the context of international commercial arbitration would be not to require without exception that the award be signed by all arbitrators but to prescribe that the fact of a missing signature and the reason therefor be stated in the award and that at least a majority of the arbitrators have signed the award.

87. Another issue to be considered is whether the model law should establish any requirements as to the contents of the award.<sup>32</sup> Some such elements might be viewed as being too obvious to be expressly stated in the law, for example, the operative part (decision), the names and addresses of the parties and of the arbitrators, and the subject-matter of the dispute. However, there are points which may be less obvious but very important, for example the place and the date of the award. Finally, there is a point to be included on which national laws differ and which is controversial, that is

whether the award shall state the reasons on which it is based. Probably the most acceptable solution on the international plane would be to require such statement of reasons unless the parties have agreed that no reasons are to be given.

### 4. Pleas as to arbitrator's jurisdiction

88. The arbitral tribunal should be empowered to decide itself about any pleas as to its jurisdiction. In particular, it should have the power to determine the existence and validity of the arbitration agreement. If the agreement is set forth in an arbitral clause, the determination of the arbitral tribunal's "competence-competence" would be facilitated by the separability of that clause as discussed earlier (paragraph 58).

89. A difficult question remains, that is, whether the decision of the arbitral tribunal about its jurisdiction shall be final or whether it shall be subject to review by a court. In support of court control, one may argue that the arbitrators cannot have the final say on their competence since their jurisdiction is to the exclusion of court jurisdiction. If one would follow this line of thinking, although it may be deemed less convincing in the international context, one might consider imposing some restriction on the right to ask for review by a court. For example, article 18 (3) of the Strasbourg Uniform Law provides that "the arbitral tribunal's ruling that it has jurisdiction may not be contested before the judicial authority except at the same time as the award on the main issue and by the same procedure".

### 5. Law applicable to substance of dispute

90. The first question is to what extent arbitrators ought to observe rules of law in deciding the dispute. It is suggested that the model law recognize an agreement by the parties that the arbitrators shall decide as "*amiables compositeurs*" (or "*ex aequo et bono*"). It would be helpful, though difficult, to define such mandate, for example, along the following lines: *Amiables compositeurs* must observe those mandatory provisions of law regarded in the respective country as ensuring its (international) *ordre public*. In view of the commercial context, it may be added that the arbitrators, whether or not acting as *amiables compositeurs*, shall decide in accordance with the terms of the contract, taking into account the pertinent trade usages.

91. The model law may also empower the arbitral tribunal to determine what law is applicable to the dispute unless the parties have designated a certain law to be applied. As to the facility of designating a law, the model law might recognize not only the choice of a specific national law but also allow reference to a uniform law or convention even if not yet in force. It may also be useful, as mentioned earlier (paragraph 24), to include a provision to the effect that any choice of the law of a given

<sup>31</sup> In addition to this sanction, the 1966 Strasbourg Uniform Law even envisages termination of the arbitration agreement if the arbitrators are named therein (see above, para. 62).

<sup>32</sup> Cf. e.g. article 22 (5) and (6) of the 1966 Strasbourg Uniform Law:

"5. An award shall, in addition to the operative part, contain the following particulars: (a) the names and permanent addresses of the arbitrators; (b) the names and permanent addresses of the parties; (c) the subject-matter of the dispute; (d) the date on which the award was made; (e) the place of arbitration and the place where the award was made.

"6. The reasons for an award shall be stated."

State means direct reference to the substantive law of that State and not to its conflicts rules.

#### 6. Settlement

92. Where parties, as is often the case, during arbitration proceedings reach an amicable settlement of their dispute, questions arise as to the form and legal status of such settlement. While national laws and arbitration rules provide varied answers, an acceptable approach could be that the model authorize, but not compel, the arbitral tribunal to record such a settlement in the form of an award on agreed terms ("*accord des parties*"). Then, it would have to be decided whether such an award should be treated, e.g. as regards registration, enforcement, or any recourse, exactly like a "normal" award or whether any special regulations seem necessary.

#### 7. Correction and interpretation of award

93. It might be useful to include a provision according to which a party may request within a certain period of time that the arbitral tribunal give an interpretation of the award or correct certain errors (cf. e.g. articles 35 and 36 of the UNCITRAL Arbitration Rules). Such a provision, though of limited importance, could help to overcome any problems arising from the fact that the mandate of the arbitral tribunal is terminated by making the award.

#### 8. Fees and costs

94. Provisions relating to the costs of arbitration, including the arbitrators' fees, are usually contained in the arbitration agreement by way of reference to standard arbitration rules which may set forth fee schedules or the procedures of fixing the respective amounts. There seems to be little that the model law should regulate in that regard. Perhaps it could specifically mention the right to request deposits which is of practical importance in the international context. Also, it might authorize the arbitrators, subject to any rule adopted by the parties, to fix their own fees, possibly with some provision for review by a court.

#### 9. Delivery and registration of award

95. It is clear that the award has to be delivered to the parties, whereby copies signed by the arbitrators or duly certified copies could be used. Such delivery or notification should be required under the model law since it is one condition for the final and binding nature of the award which, in turn, is a condition for its enforcement.

96. Another condition is, under a substantial number of national laws, that the award, normally the authenticated original, is registered or deposited with a certain court or office, differently designated in different States. It will have to be considered whether the model law

should require such deposit although it is not found in all national laws and, where it is found, its regulation varies widely as regards form, procedure and competent authority. Another possible reason against such a requirement relates to the fact that the deposit, where it is required, is primarily needed for the enforcement of the award. Here, special considerations come into play with regard to the model law to be discussed now.

#### 10. Executory force and enforcement of award

97. National laws commonly provide that the award obtains its executory force by an "*exequatur*" (leave for enforcement), whereby the particulars of the procedure and the authority giving the order vary from one State to the other. When drafting corresponding provisions of the model law, the special scope of application must be taken into account and its relationship to the scope of the 1958 New York Convention. If, for example, enforcement of an award made in (and under the law of) State X is sought in State Y, no "*exequatur*" is needed in State X (and, thus, no deposit there for that purpose) under the 1958 New York Convention whose major achievement was to abolish the requirement of a double-*exequatur*. If enforcement of that same award is sought in the country of origin itself (State X), then the 1958 New York Convention is not applicable and the model law would remain as the governing law.

98. Conceivably, the provisions of the different national laws on enforcement of domestic awards could provide the basis for drafting acceptable rules for the model law which, then, would probably include deposit of the award as a requirement for the *exequatur*. However, looking back at the two situations described in the preceding paragraph, a different approach is suggested here: To the extent possible, the two situations should be treated alike and, therefore, the model law should adopt the same conditions and procedures as laid down in the 1958 New York Convention for the enforcement of "foreign" awards. This approach, which should also be followed with regard to any means of recourse (see below, paragraphs 105-111), would enhance unification and, thus, facilitate matters in a field of great practical importance. It would also underline the international character of the arbitrations covered by the model law and clearly separate them from purely domestic cases.

99. If it were decided to follow this approach, the provisions of the 1958 New York Convention, in particular articles III and IV, would determine the direction to be taken in drafting enforcement rules for the model law:

#### "Article III

"Each Contracting State shall recognize arbitral awards as binding and enforce them in accordance with the rules of procedure of the territory where the

award is relied upon, under the conditions laid down in the following articles. There shall not be imposed substantially more onerous conditions or higher fees or charges on the recognition or enforcement of arbitral awards to which this Convention applies than are imposed on the recognition or enforcement of domestic arbitral awards."

#### "Article IV

"1. To obtain the recognition and enforcement mentioned in the preceding article, the party applying for recognition and enforcement shall, at the time of the application, supply:

"(a) The duly authenticated original award or a duly certified copy thereof;

"(b) The original agreement referred to in article II or a duly certified copy thereof.

"2. If the said award or agreement is not made in an official language of the country in which the award is relied upon, the party applying for recognition and enforcement of the award shall produce a translation of these documents into such language. The translation shall be certified by an official or sworn translator or by a diplomatic or consular agent."

100. The reference, in article III, to "the rules of procedure of the territory where the award is relied upon" shows that the Convention itself does not fully regulate the procedure. Consequently, some such procedural rules would have to be included in the model law. In order to meet the requirement imposed by article III concerning the "onus" placed on a party seeking recognition and enforcement, these provisions should envisage a procedure as simple and easy as possible. The provisions would have to determine the competent authority and its procedure while the obligations placed on the applying party are to be regulated as in article IV. In view of the requirement under article IV that the applying party supply the duly authenticated original award or a duly certified copy thereof, one may consider not to require deposit of the award after it is made by the arbitral tribunal. This way, full alignment could be achieved with the desirable result that in practice it would not matter whether recognition and enforcement of an "international" award is sought in the country of origin or somewhere else.

#### 11. Publication of award

101. It may be doubted whether the model law should deal with the question whether an award may be published. Although it is controversial, since there are good reasons for and against such publication, the decision may be left to the agreement of the parties or the arbitration rules chosen by them. If, nevertheless, a provision were to be included, probably an acceptable com-

promise could be that the award may be made public only with the express consent of the parties.

### VI. Means of recourse

#### 1. Appeal against arbitral award

102. The question whether an appeal may lie from the arbitral award is relevant to the question at what point of time an arbitral award obtains "the authority of *res judicata*", as it is called in article 24 of the 1966 Strasbourg Uniform Law, or becomes binding on the parties which is one of the conditions for the award to be enforceable (cf. article V (1) (e) 1958 New York Convention). As regards appeal to any (second instance) arbitral tribunal, the answer seems simple. The model law should recognize any such appeal if agreed on by the parties, as is not uncommon in commodity arbitrations.

103. The answer is more difficult, however, in respect of any appeal to the courts. Such judicial review on the merits, at least on certain questions of law, is envisaged under some national laws. Yet, as illustrated by the recent change concerning the most prominent example, the "special case procedure" under United Kingdom law,<sup>33</sup> there is a clear trend towards further limiting the control function of the courts in the international context. This development is based on the same considerations as the trend to restrictively apply any public policy ground, and that is the realisation of the specific features of international commercial arbitration, in particular, its limited connexion to any given domestic legal system.

104. It is suggested, therefore, that judicial control on the merits be limited to the utmost. There are, of course, certain minimum standards which any State wants to see observed even in international arbitrations. However, these standards which form part of its international *ordre public*, including any restrictions as to the arbitrability of the subject matter, do not necessitate any appeal procedure. They could, and it is submitted should, be appropriately taken care of in any setting aside procedures or, as envisaged under article V (2) of the 1958 New York Convention, in procedures relating to recognition and enforcement of the award. As to the method of excluding appeals to courts, one might consider envisaging a respective "exclusion agreement" by the parties. Yet, it would be clearer and more effective to exclude any appeal to courts expressly by the model law.

#### 2. Remedies against leave for enforcement (exequatur)

105. As regards remedies against leave for enforcement, similar considerations apply as have been set forth above with regard to executory force and enforcement (paragraphs 98-100). In particular, the same approach of

<sup>33</sup> For an account of the changes, see Schmitthoff, *op. cit.* (footnote 14), pp. 233-237.

aligning the requirements and procedures of the model law with the provisions of the 1958 New York Convention may be recommended here. The desirable result would be that in practice recognition and enforcement could be successfully objected to by a party, and would be refused, on essentially identical grounds irrespective of whether enforcement is sought in the country of origin or somewhere else. The only difference, which is justified and already inherent in the 1958 New York Convention, arises from the fact that the reasons set forth in paragraph (2) of article V relate to the law of the State of enforcement and may, thus, lead to divergent results.

106. If this "internationalist" approach, for the sake of uniformity, would be adopted, the reasons on which a remedy against leave for enforcement could be based under the model law would be those laid down in article V of the 1958 New York Convention. In addition to the rules on the reasons, the model law would have to regulate the procedure to be followed by a party objecting to the leave for enforcement. It would probably envisage resort to the same authority as the one granting the *exequatur*, possibly allowing further recourse (appeal) to a higher instance.

### 3. *Setting aside or annulment of award (and similar procedures)*

107. The issues relating to setting aside or annulment of arbitral awards are amongst the most difficult ones to be settled in the model law. It is also submitted that the pertinent provisions to be drafted will have a decisive influence on the value of the model law as a legal regime exclusively geared to international arbitrations. This is particularly true with regard to the grounds on which an application for the setting aside or annulment of an award may be based. To some extent, it is also true with regard to the procedures envisaged under domestic laws.

108. To start with the minor problem, i.e. the procedure, there is a great variety in national laws of different claims for "attacking" an award, not only for setting aside or, sometimes treated separately, annulment of the award but also to other aims, e.g. suspension or reinstatement.<sup>34</sup> The disparities extend to procedural particulars such as form, time-limits, and competent authority. For the sake of uniformity which would facilitate international practice as regards the post-award stage, an attempt should be made to establish commonly acceptable procedures, in particular, to provide for only one type of application and proceedings, probably to be called "setting aside procedures".

109. The most important point, however, would be to determine the grounds on which such application for

setting aside may be based. National laws often contain rather extensive and elaborate lists of reasons upon which a dissatisfied party may rely. While some of these reasons may be easily disregarded as being geared to specific domestic situations or of minimal practical relevance, it will not be an easy task to agree on the reasons to be included in the model law. Yet, it is suggested that every effort be made to limit the number of reasons to the extent acceptable.

110. Ideally, one should aim at a list, shorter than the one set forth in the 1966 Strasbourg Uniform Law,<sup>35</sup> that would contain only those reasons on which recognition and enforcement may be refused under the 1958 New York Convention, i.e. article V (1), (a)-(d) and (2). This restrictive approach, adopted in article IX of the 1961 European Convention for enforcement purposes,<sup>36</sup> would meet the concerns underlying the cor-

#### <sup>35</sup> Article 25:

"1. An arbitral award may be contested before a judicial authority only by way of an application to set aside and may be set aside only in the cases mentioned in this Article.

"2. An arbitral award may be set aside:

"(a) If it is contrary to *ordre public*;

"(b) If the dispute was not capable of settlement by arbitration;

"(c) If there is no valid arbitration agreement;

"(d) If the arbitral tribunal has exceeded its jurisdiction or its powers;

"(e) If the arbitral tribunal has omitted to make an award in respect of one or more points of the dispute and if the points omitted cannot be separated from the points in respect of which an award has been made;

"(f) If the award was made by an arbitral tribunal irregularly constituted;

"(g) If the parties have not been given an opportunity of substantiating their claims and presenting their case, or if there has been disregard of any other obligatory rule of the arbitral procedure, in so far as such disregard has had an influence on the arbitral award;

"(h) If the formalities prescribed in paragraph 4 of Article 22 have not been fulfilled;

"(i) If the reasons for the award have not been stated;

"(j) If the award contains conflicting provisions.

"3. An award may also be set aside:

"(a) If it was obtained by fraud;

"(b) If it is based on evidence that has been declared false by a judicial decision having the force of *res judicata* or on evidence recognised as false;

"(c) If, after it was made, there has been discovered a document or other piece of evidence which would have had a decisive influence on the award and which was withheld through the act of the other party.

"4. A case mentioned in sub-paragraph (c), (d) or (f) of paragraph 2 shall be deemed not to constitute a ground for setting aside an award where the party availing himself of it had knowledge of it during the arbitration proceedings and did not invoke it at the time.

"5. Grounds for the challenge and exclusion of arbitrators provided for under Articles 12 and 14 shall not constitute grounds for setting aside within the meaning of paragraph 2 (f) of this Article, even when they become known only after the award is made."

#### <sup>36</sup> Article IX:

"1. The setting aside in a Contracting State of an arbitral award covered by this Convention shall only constitute a ground for the refusal of recognition or enforcement in another Contracting State where such setting aside took place in a State in which, or under the law of which, the award has been made and for one of the following reasons:

"(a) the parties to the arbitration agreement were under the law applicable to them, under some incapacity or the said agreement is not valid under the law to which the parties have subjected it or,

<sup>34</sup> The manifold types of remedies are listed in the national reports, published in YCA, under chapter VI, 5.



responding proposal of the International Chamber of Commerce which is contained in the "list of subject-matters for possible inclusion in the future work programme" considered by the Commission at its eleventh session.<sup>37</sup> It would help to prevent that an international award falls victim to local particularities of law although the case at hand bears no substantive connexion with that respective State.

111. If this recommendation were followed, it would result in full alignment of the reasons for setting aside and for refusing recognition and enforcement. Nevertheless, the setting aside procedure would not become superfluous since it would allow a party to raise objections against an international award in the country where, or under the law of which, it was made irrespective of whether enforcement is sought there by the other party. At the same time, the respective State (of origin) would have a chance of "monitoring" observance by arbitrators active within its boundaries of its pro-

failing any indication thereon, under the law of the country where the award was made; or

"(b) the party requesting the setting aside of the award was not given proper notice of the appointment of the arbitrator or of the arbitration proceedings or was otherwise unable to present his case; or

"(c) the award deals with a difference not contemplated by or not falling within the terms of the submission to arbitration, or it contains decisions on matters beyond the scope of the submission to arbitration, provided that, if the decisions on matters submitted to arbitration can be separated from those not so submitted, that part of the award which contains decisions on matters submitted to arbitration need not be set aside;

"(d) the composition of the arbitral authority or the arbitral procedure was not in accordance with the agreement of the parties, or failing such agreement, with the provisions of Article IV of this Convention.

"2. In relations between Contracting States that are also parties to the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards of 10th June 1958, paragraph 1 of this Article limits the application of Article V (1) (e) of the New York Convention solely to the cases of setting aside set out under paragraph 1 above."

<sup>37</sup> Report of the United Nations Commission on International Trade Law on the work of its eleventh session, *Official Records of the General Assembly, Thirty-third Session, Supplement No. 17* (A/33/17), para. 41, sub. I (e) (iii) (Yearbook . . . 1978, part one, II, A).

visions of law to the extent they are mandatory for international cases.

#### CONCLUSION AND SUGGESTED COURSE OF ACTION

112. This report does not discuss in detail all the issues and considerations relevant in the preparation of a model law. It is hoped, though, that it provides a sufficient basis for the Commission to decide on its future course of action in respect of this project. It may be concluded that the preparation of a model law on international commercial arbitration is desirable in view of the manifold problems encountered in present arbitration practice and the above-stated concerns which could be met by a widely acceptable law. It also seems to be the appropriate time for such an undertaking since international arbitrations are increasing and there are intentions in a number of States to adopt legislation geared thereto.

113. On the basis of this report, the Commission may wish to discuss the general concerns and principles that would underlie the model law. It may also wish to discuss the issues identified in the report and the pertinent recommendations as to the most suitable approaches to be taken. Such an exchange of views which would help to determine the direction, in particular, as regards the scope and probable contents of the law seems necessary before a first draft of the model law can be prepared.

114. In view of the complexity of the issues and the work required for the preparation of a draft model law, the Commission may wish to entrust a Working Group with that task. Because of budgetary restrictions, it may be considered to give that mandate to the Working Group on International Contract Practices which has completed its task. The Working Group might use this report as its agenda, probably starting with the arbitration agreement, and should follow the directions given by the Commission at this session. It would then, assisted by the Secretariat and in consultation with interested organizations, prepare draft provisions to be submitted to the Commission at a later session.



## IV. NEW INTERNATIONAL ECONOMIC ORDER\*

### A. Report of the Working Group on the New International Economic Order on the work of its second session held at Vienna, 9-18 June 1981: clauses related to contracts for the supply and construction of large industrial works (A/CN.9/198)\*\*

#### INTRODUCTION

1. At its eleventh session the United Nations Commission on International Trade Law decided to include in its work programme a topic entitled "The legal implications of the new international economic order" and established a Working Group to deal with this subject.<sup>1</sup>

2. At its twelfth session the Commission designated member States of the Working Group.<sup>2</sup> The Working Group held its first session in New York from 14 to 25 January 1980 and recommended to the Commission for possible inclusion in its work programme, *inter alia*:

"4. Harmonization, unification and review of contractual provisions commonly occurring in international contracts in the field of industrial development, such as contracts on research and development, consulting, engineering, supply and construction of large industrial works (including turn-key contracts or *contrats produits en main*), transfer of technology (including licensing), service and maintenance, technical assistance, leasing, joint venture, and industrial co-operation in general."<sup>3</sup>

3. At its thirteenth session the Commission decided that the Working Group should be composed of all States members of the Commission and agreed to accord priority to work related to contracts in the field of industrial development. The Secretariat was requested to carry out preparatory work in respect of contracts on supply and construction of large industrial works and on industrial co-operation.<sup>4</sup>

\* For consideration by the Commission see Report, chapter V (part one, A, above).

\*\* 19 June 1981. Referred to in Report, para. 71 (part one, A, above).

<sup>1</sup> Report of the United Nations Commission on International Trade Law on the work of its eleventh session, *Official Records of the General Assembly, Thirty-third Session, Supplement No. 17* (A/33/17), para. 71 (Yearbook . . . 1978, part one, II, A).

<sup>2</sup> Report of the United Nations Commission on International Trade Law on the work of its twelfth session, *Official Records of the General Assembly, Thirty-fourth Session, Supplement No. 17* (A/34/17), para. 100 (Yearbook . . . 1979, part one, II, A).

<sup>3</sup> A/CN.9/176, para. 31 (Yearbook . . . 1980, part two, V, A).

<sup>4</sup> Report of the United Nations Commission on International Trade Law on the work of its thirteenth session, *Official Records of the General Assembly, Thirty-fifth Session, Supplement No. 17* (A/35/17), para. 143 (Yearbook . . . 1980, part one, II, A).

4. The Working Group held its second session at Vienna, from 9 to 18 June 1981. All the members of the Working Group were represented except Burundi, Colombia, Cuba, Cyprus, Peru, Senegal and Sierra Leone.

5. The session was attended by observers from the following Governments: Argentina, Belgium, Brazil, Bulgaria, Canada, China, Ecuador, Gabon, Malaysia, Netherlands, Pakistan, Republic of Korea, Romania, Suriname, Sweden, Switzerland, Thailand, Togo, Tunisia, Turkey, Uruguay and Venezuela.

6. The session was attended by observers from the following United Nations Organs: Centre on Transnational Corporations, Economic Commission for Africa, United Nations Industrial Development Organization and the United Nations Institute for Training and Research.

7. The session was also attended by observers from the following international governmental and non-governmental organizations: Commission of the European Communities, European Free Trade Association, Hague Conference on Private International Law, International Association of Democratic Lawyers, International Bar Association and International Chamber of Commerce.

8. The Working Group elected the following officers:

Chairman: ..... Mr. Leif Sevón (Finland)

Rapporteur: ..... Mr. Stephen K. Muchui (Kenya)

9. The Working Group had before it the Study of the Secretary-General entitled "Clauses related to contracts for the supply and construction of large industrial works" (A/CN.9/WG.V/WP.4 and Add. 1 to 8)\* and a note on "Clauses related to industrial co-operation" (A/CN.9/WG.V/WP.5).\*\*

10. The Working Group adopted the following agenda:

(a) Election of officers

(b) Adoption of the agenda

\* Reproduced in this volume, part two, IV, B, 1.

\*\* Reproduced in this volume, part two, IV, B, 2.

(c) Consideration of contracts for the supply and construction of large industrial works and on industrial co-operation

(d) Other business

(e) Adoption of the Report.

#### CONSIDERATION OF CONTRACTUAL PROVISIONS RELATING TO CONTRACTS FOR THE SUPPLY AND CONSTRUCTION OF LARGE INDUSTRIAL WORKS

11. The Working Group began its deliberations with a discussion of paragraphs 39-46 of Part One of the Working Paper (A/CN.9/WG.V/WP.4) which set forth the possible directions that the work could take. There was an exchange of views on the various approaches suggested, i.e. legal guide, model clause, code of conduct, general conditions and convention.

12. There were suggestions in favour of the formulation of a legal guide. It was pointed out that this approach would be more flexible and, moreover, work of such a nature could be accomplished in a relatively short period of time. Such a guide should identify the legal issues involved and suggest possible solutions to assist parties in their negotiations.

13. It was pointed out that such a guide should not exclude model clauses. Should a model clause be included in the guide, various alternatives ought to be given. The model clause should also be practice-oriented.

14. It was pointed out that the guide was to be carefully considered in the context of the New International Economic Order (NIEO). The Working Group was in general agreement that its work should be within the context of the basic principles of NIEO and in particular should be directed to meeting the needs and aspirations of the developing countries.

15. According to a view the work of the Working Group on this subject, in view of its mandate, should focus on the aspect of development especially of developing countries in order to distinguish its work from the work of other Working Groups of UNCITRAL.

16. Some views were expressed that the work should be concentrated only on semi-turn-key and not turn-key contracts as the latter involved civil engineering works, which were of a specialized nature. Another view was that not only the two types of contract but also other variants of the two should be taken into consideration in the formulation of the guide as this would involve a discussion of all issues pertaining to a works contract. It was observed that in the discussion of any issue, the different types of contract would have to be taken into consideration.

17. A point was raised as to whether the Group was duplicating the work currently undertaken by the United

Nations Industrial Development Organization (UNIDO) in respect of model contracts for the construction of fertilizer plants. It was pointed out that the work envisaged by the UNCITRAL Working Group was to be of a wider scope and was to take into consideration all types of industries.

18. Further, it was pointed out that other organs within the United Nations were also engaged in some aspects of industrial contracts. In this context it was observed that the question of co-ordination was of utmost importance. As UNCITRAL is a core legal body in the field of international trade law the preparation of a legal guide would be of assistance to other organs in considering certain legal issues involved in industrial contracts. In this way unification and harmonization may be attained in this area.

19. The work envisaged by the UNCITRAL Working Group was to be of a more comprehensive legal nature. There was general consensus that it would be useful as a first practical step to undertake the formulation of a detailed legal guide covering turn-key and semi-turn-key contracts as well as their variants. Problems posed by various clauses would be examined in the context of such contracts. Also, the advantages and disadvantages of various alternative solutions to such problems, if any, would be indicated.

20. The Working Group then turned to a discussion and preliminary exchange of views on particular topics based on the documentation provided by the Secretariat. The purpose of this discussion, as summarized in the following sections,<sup>5</sup> was to provide indications to the Secretariat for drafting a guide and not to draft specific recommendations on the final contents of the guide.

#### EXONERATION<sup>6</sup>

21. The opinion of the Working Group was divided in respect of the definition of exoneration. One view favoured a general definition based on "exemptions" as defined in article 79 of the United Nations Convention on Contracts for the International Sale of Goods (Sales Convention). It was pointed out that the Sales Convention applied to sale of goods only, while the legal guide was to deal with contracts for large industrial works. Another view favoured an exhaustive list. There was yet another suggestion to have a combination of a general definition followed by an illustrative list of exonerating circumstances.

<sup>5</sup> Summaries of debates on specific legal issues are set out below in the order of discussion. This order was decided after taking into account the availability of the basic documents, and the complexity of the subjects and their relationship with one another.

<sup>6</sup> A/CN.9/WG.V/WP.4/Add.5: paras. 1-48 (reproduced in this volume, part two, IV, B, 1). A/CN.9/WG.V/WP.4/Add.8: paras. 98-113 (reproduced in this volume, part two, IV, B, 1).

22. There was wide agreement that exonerating circumstances stipulated in a contract should be few and of an exhaustive nature. It was thought undesirable to admit other exonerating circumstances on the basis of applicable law. It was, however, observed that the rules of applicable law might be of a mandatory character. It was suggested that the question of "economic" difficulties should be dealt with in a "hardship" clause, and not in an exoneration clause, subject to the definition of the terms.

23. The Working Group was of the opinion that the failure to notify the other party of an exonerating event should not entail loss of the right to rely on the event. However, if notice of the impediment was not given to the other party, the non-performing party should be liable for damages resulting from the failure to give such notice.

24. The opinion of the Working Group was divided on the question of the consequences of exoneration. The view was expressed that the special nature of contracts for the supply and construction of large industrial works should be taken into consideration. Thus instead of terminating the contract there should be only a suspension of the contract if the impediment was not permanent.

25. It was observed that a distinction should be made between a partial and total failure of performance. A factor also to be taken into consideration should be the stage at which the impediment occurred. In the guide, different solutions should be indicated. The view was expressed that the consequences of exoneration should be limited to the exclusion of damages and problems concerning termination of the contract should be dealt with in the chapter on termination. There was general agreement that the termination of a contract should be the last solution.

#### RENEGOTIATION<sup>7</sup>

26. The Working Group was of the opinion that the question of renegotiation should be discussed in the guide in cases where an exonerating event temporarily suspended the obligations of the parties if this was felt useful. The purpose of renegotiation would be to adapt the contract to changed circumstances.

27. Some views were expressed as to the methodology of renegotiation. It was suggested that the guide should list various possibilities to assist the parties in their renegotiation, pointing to the advantages and disadvantages of each approach. There was also a suggestion that provision should be made as to the consequences if one of the parties refused to participate in the renegotiation. Conciliation and arbitration were mentioned as possible

procedures that parties could resort to in order to assist them in their renegotiation.

28. The Working Group noted that another area in which renegotiation of a contract could be provided for to adapt the contract to changed circumstances was in hardship situations. The Working Group proceeded first to consider whether the insertion of a hardship clause in a works contract should be encouraged. Opinion was divided on this question.

29. In favour of inclusion it was argued that a works contract was one of complexity and of long duration. Changed circumstances may arise to affect the contractual equilibrium of the parties and cause hardship if the contract were to be continued under its original terms. It was also felt that a hardship clause could assist not only the contractor but also the purchaser to alleviate the hardship.

30. According to another view a hardship clause was to be approached with great caution. It was observed that at the present moment the concept of "hardship" was still unclear and ill-defined. There might be the danger that it would be used by a contractor in a developed country to escape his obligations under a contract to the disadvantage of a purchaser in a developing country. For this reason there was also opposition against any inclusion of a hardship clause. It was pointed out that any business would involve a risk element and to allow a party to signal for renegotiation in a "hardship" situation would not be conducive to the certainty of a contract.

31. Despite some doubts expressed on the usefulness of a hardship clause, there was general consensus that the legal guide should deal with such a clause, but pointing to its advantages and disadvantages.

32. It was generally agreed that a hardship clause should be distinguished from a price revision clause which raised special problems. It was noted that the subject of price revision was to be considered in a separate chapter.

33. The Working Group was of the view that an attempt should be made in the guide to lay down clearly the criteria for the recognition of a hardship situation that would bring about renegotiation of the contract. The guide should also spell out the position of the contract during renegotiation and consider the various consequences relating to the performance of the contract, bearing in mind the sort of situations that had given rise to the renegotiation.

#### QUALITY<sup>8</sup>

34. The Working Group was of the opinion that the question of quality was very important and that detailed

<sup>7</sup> A/CN.9/WG.V/WP.4/Add.5: paras. 49-79 (reproduced in this volume, part two, IV, B, 1). A/CN.9/WG.V/WP.4/Add.8: paras. 114-123 (reproduced in this volume, part two, IV, B, 1).

<sup>8</sup> A/CN.9/WG.V/WP.4/Add.2: paras. 38-74 (reproduced in this volume, part two, IV, B, 1). A/CN.9/WG.V/WP.4/Add.8: paras. 50-55 (reproduced in this volume, part two, IV, B, 1).

provision should be made in the contract itself. In dealing with this question, a distinction between turn-key and other types of contracts should be taken into consideration.

35. Different views were expressed as to whether the contractor should be obliged, if necessary, to conform to a higher standard requirement according to the law of the country in which the plant was to be erected. A view was expressed that the contents of the contract ought to be decisive. Another view was expressed that the contractor should conform to a higher standard if required by the law of the country where the plant was to be erected, the purchaser bearing the extra cost, if any. It was suggested that the purchaser should advise the contractor of such standards in any case.

#### INSPECTION AND TESTS<sup>9</sup>

36. It was observed that the purpose of inspection and tests was to ensure that the plant would meet the quality and conform to specifications expected under a works contract. Defects discovered, on inspection, during production would reduce the costs of remedying the defects and avoid delays. Tests conducted after completion would demonstrate whether the performance of the plant was in accordance with the terms of the contract. It was pointed out that the interests of both the contractor and the purchaser would be served from such an exercise.

37. After deliberation, the Working Group recommended that the following matters be considered in the guide:

Costs of inspection and tests.

Right of the purchaser to reject defective materials.

Provision of the necessary facilities by the contractor for the purpose of carrying out inspection and tests.

Detailed specification of the kinds of inspection and tests that are to be carried out.

Indication regarding parts of plant that are not to be inspected or tested.

Desirability of "joint" inspection and tests.

Provision for third party intervention, e.g. appointment of an engineer to assist the parties in the event of disagreement as to whether or not the plant was defective.

38. Diametrically opposite views were expressed as to whether the nature of a contract, e.g. turn-key or semi-turn-key, would affect the rights and obligations of the parties regarding inspection and tests.

<sup>9</sup> A/CN.9/WG.V/WP.4/Add.3: paras. 1-90 (reproduced in this volume, part two, IV, B, 1). A/CN.9/WG.V/WP.4/Add.8: paras. 56-67 (reproduced in this volume, part two, IV, B, 1).

39. It was observed that the guide should deal with performance tests, as these tests were not provided for sufficiently in existing contracts for the supply and construction of large industrial works.

40. There was a suggestion that the guide should contain illustrative forms with respect to certificates of inspection and tests and that UNCITRAL should attempt to unify and simplify such certificates.

41. Divergent views were expressed as to what remedies would be available to the purchaser if the materials or the plant were found to be defective during the course of inspection and tests. According to one view, the legal effects of non-conformity should not apply at this stage. However, the purchaser should be able to require the contractor to repair the defects or replace with new materials and/or plant. According to another view, the purchaser should be entitled to reject the materials and/or plant even at the stage of production.

42. There was general consensus that the purchaser should not lose his right to have the defects repaired even if he did not indicate any defects or if he did not undertake the inspection and tests during construction.

#### COMPLETION<sup>10</sup>

43. There was general agreement that the notion of "completion" was not quite clear and it was desirable to clarify it in the guide. It was stressed that this term did not necessarily mean that the contract was completed. The view was expressed that "completion" was to be interpreted as the mechanical completion of the work or the physical completion relating to the erection of works. There was consensus that it was advisable to define "completion" in a works contract, particularly in connexion with the programme relating to construction of works.

44. General support was expressed for an explanation or definition of the main terms used in the guide in order to assist the understanding of such terms. In this connexion a distinction between individual stages of the construction of the plant would be desirable.

#### TAKE-OVER AND ACCEPTANCE<sup>11</sup>

45. The Working Group noted that the concepts of "take-over" and "acceptance" were not interpreted in the same way. The view was expressed that these terms

<sup>10</sup> A/CN.9/WG.V/WP.4/Add.3: paras. 91-104 (reproduced in this volume, part two, IV, B, 1). A/CN.9/WG.V/WP.4/Add.8: paras. 68-74 (reproduced in this volume, part two, IV, B, 1).

<sup>11</sup> A/CN.9/WG.V/WP.4/Add.3: paras. 105-133 (reproduced in this volume, part two, IV, B, 1). A/CN.9/WG.V/WP.4/Add.8: paras. 75-80 (reproduced in this volume, part two, IV, B, 1).

should not be distinguished as they determined the time of the passing of risk and commencement of a guaranty period. On the other hand, it was observed that such a distinction might be useful. It was pointed out that "take-over" should mean the taking possession of the work and "acceptance", the approval of the work.

46. There was general agreement that definitions of the above terms should be determined in the contract itself and their legal consequences should be made clear. Taking into consideration the need to simplify and clarify individual stages of construction, it was noted that it would be advisable to recommend a distinction between "take-over" and "acceptance" in the guide in case of a need for such a distinction in order to determine clearly the legal position of the parties.

47. It was suggested that the question of hidden defects of the plant might be raised even after the acceptance of the work, but not apparent defects.

48. It was requested that problems concerning presumed acceptance as well as partial and provisional acceptance should be dealt with in the guide.

#### GUARANTIES<sup>12</sup>

49. There was general agreement that guaranty was one of the most important issues to be dealt with in the guide. It was stressed that at this juncture the Working Group would deal only with guaranties concerning plants, and would defer consideration of bank and other guaranties, including performance bonds.

50. The opinion of the Working Group was divided on the question whether it was advisable to distinguish between mechanical guaranty and performance guaranty or whether it would be preferable to have a single guaranty only, covering both materials, design and workmanship, and proper performance of the works.

51. Different views were expressed in respect of the length of a guaranty period. It was observed that a guaranty period for a considerable length of time was needed for the developing countries. It was suggested that it would be desirable to have a guaranty period for one third of the life expectancy of a plant. It was pointed out that the life of a plant, its usage, maintenance and changes in technology and skill of personnel were factors to be taken into consideration. It was observed that the length of the guaranty period might influence the price of the plant.

52. There was wide support for the view that the length of the guaranty period was to be settled by the parties in the contract and that the guide should draw

attention of the parties to the legal aspects that might determine their legal position.

53. It was suggested that in preparing the guide, general conditions applied to contracts for the supply of large industrial works by member States of the Council for Mutual Economic Assistance, among others, should also be taken into consideration.

54. It was pointed out that the guide should deal with the legal consequences of the breach of guaranty by the contractor. Furthermore, it was important to consider whether the expiration of the guaranty period would exempt the contractor completely from any further obligations.

55. It was observed that questions of assurance of supply of spare parts and adequate training of personnel for the operation of the plant were also important. It was noted in this connexion that the second part of the study of the Secretariat, to be submitted to the next session of the Working Group, would cover these subjects.

#### RECTIFICATION OF DEFECTS<sup>13</sup>

56. It was noted that the term "defects" was not clear and that it should be clarified in the guide. In considering this term, it was suggested that consideration should be given to other notions such as "faults", "non-conformity" and "omissions". A clear distinction should also be made between different types of defects, whether they be major or minor, as this would affect the legal consequences.

57. Divergent views were expressed as to whether a distinction should be made between rectification of defects during production and after taking-over.

58. In favour of the distinction it was argued that as the plant was in the hands of the contractor during production the purchaser should not have the right to reject as the contractor could still repair the defects and supply a plant in conformity with the terms of the contract. However, if the defects were discovered at take-over, the purchaser would have the right to reject. After taking-over and acceptance the purchaser would only have the right of rectification.

59. In favour of the view that no distinction should be made between the stages of production and take-over, the argument was proffered that the legal consequences should be the same, i.e. the contractor should be responsible in handing over a plant in accordance with the contract. Otherwise, the contractor would be liable for damages and the purchaser would have the right to reject the plant or have it rectified.

<sup>12</sup> A/CN.9/WG.V/WP.4/Add.6: paras. 1-72 (reproduced in this volume, part two, IV, B, 1). A/CN.9/WG.V/WP.4/Add.8: paras. 124-133 (reproduced in this volume, part two, IV, B, 1).

<sup>13</sup> A/CN.9/WG.V/WP.4/Add.2: paras. 73-118 (reproduced in this volume, part two, IV, B, 1). A/CN.9/WG.V/WP.4/Add.8: paras. 134-140 (reproduced in this volume, part two, IV, B, 1).

60. The question was also raised as to which party should be given the choice of the means of rectification. One view favoured giving the right to the contractor to decide on the measures to be taken, while another view favoured giving the choice to the purchaser.

61. On the question of notification, there was general consensus that notification was required when defects were discovered after take-over. Some views were expressed that failure to notify should not disentitle the purchaser from claiming any remedies but should only affect the question of damages. Notification should be given within a reasonable time after discovery of the defects.

62. However, there was a difference of opinion as to whether notification was necessary before take-over. It was observed that in practice the purchaser would in any event notify the contractor of the defects during production. If the purchaser were to follow the various stages of production and did not discover the defects during this period he was still entitled to have the plant in accordance with the contract. No question of notification would arise.

63. The point was raised that the legal guide should provide guidance as regards the time when the defects should be rectified as well as a possibility of utilizing a third independent party in assessing the extent of a defect.

64. It was also suggested that, besides examining various stages where defects might arise, an over-all analysis of the effects of defects should be described.

#### DELAYS AND REMEDIES<sup>14</sup>

65. It was observed that the guide should stress the importance of providing in the contract for the stipulation of the programme and time-schedule for construction of works. Also the consequences of non-compliance with the programme and time-schedule should be spelt out. It was noted that the type of contract might influence the concept of delay, in particular the question whether delay should be considered at particular stages in the construction of the works or on completion only.

66. The Working Group pointed out different views on the legal consequences of failure to make payment in time. Some views were expressed that the contractor should be entitled to suspend the performance or even terminate the contract if it was clear that the delay would continue or payment would not be made (e.g. in case of bankruptcy). On the other hand, the view was expressed that the payment of interest should be the only consequence of delay in payment. It was observed in this

connexion than an interest clause might be contrary to the applicable law. Another view favoured the same system of remedies for both parties.

67. Furthermore it was observed that the question of anticipatory breach should also adequately be covered in the guide.

#### DAMAGES AND LIMITATION OF LIABILITY<sup>15</sup>

68. In regard to liability for personal injuries and damage to property not being the subject-matter of the contract it was stressed that the contract for the supply and construction of large industrial works could not disentitle a third person (not being a party to such a contract) from claiming damages. It was observed that the only questions which might be dealt with in the guide were distribution of risks in respect of such damages and also insurance against such risks. However, it was also noted that the question of insurance was for each party to decide, and, even if this question was dealt with in the guide, the treatment should be confined to those risks which might arise from the contractual relationship. It was further noted that the Secretariat had intended to deal with insurance under a separate chapter in its future study.

69. The view was expressed that the guide should point out the relationship between the guaranty conditions and the liability of the contractor since at least in some cases the former could result in a limitation or exclusion of the latter under applicable law.

70. It was observed that there would be a general obligation to mitigate damages.

71. One view favoured only foreseeable damage. Another view was expressed that unforeseeable damage should not be excluded. There was yet another view that the relevant time for unforeseeability should not be the time of the conclusion of the contract but rather that of the breach of contract.

72. The view was expressed that the guide should stress that the validity of clauses on the limitation of contractual liability might be limited by mandatory rules of the applicable law.

73. As the notion of "damages" differed in some legal systems, the guide should make it clear what was to be understood by "direct" and "indirect" damages. In this connexion, it was observed that different types of damages, i.e. loss of profit, damage to property and personal injury should be distinguished.

74. Different views were expressed in regard to the appropriateness of the concept of gross misconduct in

<sup>14</sup> A/CN.9/WG.V/WP.4/Add.4: paras.1-22 (reproduced in this volume, part two, IV, B, 1). A/CN.9/WG.V/WP.4/Add.8: paras. 81-85 (reproduced in this volume, part two, IV, B, 1).

<sup>15</sup> A/CN.9/WG.V/WP.4/Add.4: paras. 23-52 (reproduced in this volume, part two, IV, B, 1). A/CN.9/WG.V/WP.4/Add.8: paras. 86-97 (reproduced in this volume, part two, IV, B, 1).

the ECE General Conditions which related also to loss of profits. One view was that this concept was too harsh for the purchaser. Another view considered the wording of the ECE clause as sufficient for the protection of the purchaser.

75. The Working Group was informed by the Secretary of the Commission of the work of the UNCITRAL Working Group on International Contract Practices in respect of the progress made by it on a project on liquidated damages and penalty clauses. The report of the deliberations would be submitted to the fourteenth session of UNCITRAL. The Working Group agreed that the guide should duly reflect the ultimate solution by the Commission of this matter.

#### TERMINATION<sup>16</sup>

76. There was general consensus that the termination of a contract should be the last recourse to which the parties should be entitled and only where other remedies proved inadequate. The Working Group agreed that termination of a contract should be limited only to fundamental breach. The parties should spell out very clearly in their contract the circumstances where termination could be resorted to.

77. The opinion of the Working Group was divided on the desirability of distinguishing between cases where the failure to perform was due to exonerating events and cases where either of the parties was responsible for the failure. The view was expressed that the conditions for termination of a contract should be more strict in cases where the contract was not fulfilled due to impediments for which the party was not responsible. According to another view it would not be advisable to distinguish between exonerating events and breach of contract as the termination of contract should be limited only to cases where other solutions were not possible or feasible. Such a distinction should, however, be important in respect of other legal consequences, in particular that of damages.

78. One view was expressed that the guide should also deal with the concept of partial termination making clear the legal consequences.

79. It was suggested that the term "avoidance" (in the Sales Convention) be used instead of "termination".

80. The view was expressed that the guide should also deal with possible approaches by which the purchaser could force the contractor to complete the work where the remedy of damages or termination was not adequate. Under another view there was no possibility of forcing the contractor to continue the work. However, it

would be in the interest of the contractor to complete the work otherwise his reputation might be at stake.

81. There was substantial support for the view that a notice be required for termination. However, the view was expressed that there should not be a requirement of notice in certain exceptional circumstances, e.g. abandonment of contract. In this connexion it was noted that some legal systems required an express agreement in the contract for its termination.

#### TRANSFER OF TECHNOLOGY<sup>17</sup>

82. There was general agreement to include the appropriate legal aspects of the transfer of technology in the guide. The fact that transfer of technology was also dealt with by other international organizations, particularly UNCTAD, UNIDO and WIPO, did not preclude UNCITRAL from taking up this subject. It was felt that UNCITRAL might make a contribution by resolving legal issues pertaining to the subject. Reference was made to the determination of applicable law and settlement of disputes.

83. There was also agreement that the transfer of know-how was essential in order to assist the purchaser in the operation of the plant, its maintenance and also its repair. It was pointed out that in the long run the transfer of know-how was essential to lay the basis for the industrial and technological development of developing countries. Mention was made of the need to include in the guide indications covering the possibility of the contractor employing engineers and managers of the purchasing party in all stages of work to ensure adequate transfer of technology. There were other questions involved, e.g. the training of personnel, which should be covered in the second part of the study.

84. Different views were expressed in regard to the problem of granting licences by third parties. The guide should make it clear under what conditions the contractor himself would have to provide for the technology.

85. As to the common restriction of the purchaser to sell the products of the plant in third countries the view was expressed that restrictive practices be abolished. Under another view it was argued that there might be a justification for certain restrictions.

86. Doubts were expressed as to the necessity of confidentiality in respect of all related information as found in many contracts.

87. In regard to the retransfer of technology from the purchaser to the contractor there was one view opposing such an obligation whereas another view spoke

<sup>16</sup> A/CN.9/WG.V/WP.4/Add.7: paras. 1-86 (reproduced in this volume, part two, IV, B, 1). A/CN.9/WG.V/WP.4/Add.8: paras. 141-157 (reproduced in this volume, part two, IV, B, 1).

<sup>17</sup> A/CN.9/WG.V/WP.4/Add.2: paras. 1-37 (reproduced in this volume, part two, IV, B, 1). A/CN.9/WG.V/WP.4/Add.3: paras. 38-49 (reproduced in this volume, part two, IV, B, 1).



in favour of payment for such retransfer and in favour of applying the same principle for the transfer of improvements of the technology from the contractor to the purchaser.

88. It was agreed that UNCITRAL should not duplicate the work in regard to the proposed code of conduct on transfer of technology. However, it was generally felt that it would be desirable for the legal guide to refer to relevant issues under consideration by UNCTAD so that the parties would be made aware of them.

#### FUTURE WORK

89. There was general consensus that the remaining topics listed in the study by the Secretary-General in A/CN.9/WG.V/WP.4, para. 36 should be completed by the Secretariat and examined by the Working Group.

90. It was pointed out that other topics such as maintenance, spare parts, customer's service, technical assistance, variations, financial arrangements, time limits, feasibility studies, modes and effects of notices, supply of raw materials and industrial input, tenders, liability of a consulting engineer, joint and several liability of several contractors and bankruptcy might also be included.

91. The Working Group requested the Secretariat to complete the remaining preparatory work for its next session. It was suggested that sufficient time should be made available to the Secretariat to prepare the remaining aspects of this subject in order to make the docu-

ments available well in advance to the participating countries for their study. However, the Group agreed that the Secretariat should be given a discretion regarding the organization of work including the selection of the additional topics suggested.

92. The Working Group also entrusted the Secretariat with the drafting of the legal guide.

93. As regards clauses related to industrial co-operation, the Working Group considered the note by the Secretariat on the subject (A/CN.9/WG.V/WP.5)\* and agreed that work on it be deferred. The Working Group agreed to concentrate its work on contracts for the supply and construction of large industrial works at the present moment. However, it requested the Secretariat to submit, at a future session, a preliminary study on specific features of industrial co-operation contracts after the preparation of the legal guide on contractual provisions relating to contracts for the supply and construction of large industrial works.

94. Some views were expressed on when the next session should be held. One suggestion was to hold the next session early in 1982. Another view was that the next session of the Working Group might be arranged just before the next session of the Commission as was done this time so that again many members may be represented. The Working Group expressed its wish to the Commission to take into account the urgency of the project in determining the date of the next session of the Working Group.

\* Reproduced in this volume, part two, IV, B, 2.

### B. Working papers submitted to the Working Group on the New International Economic Order at its second session (Vienna, 9-18 June 1981)

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## Part one

[A/CN.9/WG.V/WP.4\*]

## INTRODUCTION

1. The Working Group on the New International Economic Order at its session held in New York in January 1980 recommended to the Commission for possible inclusion in its work programme, *inter alia*:

"4. Harmonization, unification and review of contractual provisions commonly occurring in international contracts in the field of industrial development such as contracts on research and development, consulting, engineering, supply and construction of large industrial works (including turn-key contracts or *contrats produits en main*), transfer of technology (including licensing), service and maintenance, technical assistance, leasing, joint venture, and industrial co-operation in general."<sup>1</sup>

2. The Working Group was of the opinion that this item would be of special importance to developing countries and to the work of the Commission in the context of the new international economic order. The Group therefore requested the Secretariat to prepare a study on this item and submit it to the Commission at its thirteenth session. That study<sup>2</sup> reviewed the various types of contracts used in the context of industrialization, described their main characteristics and content and referred to the work carried out in this field by other organizations.

3. The Commission, at its thirteenth session, welcomed the recommendations of the Working Group concerning subject-matters to be included in the work programme of the Commission and agreed to accord priority to work related to contracts in the field of industrial development.<sup>3</sup>

4. In considering the various different types of contracts set forth in the study of the Secretary-General, there was wide agreement in the Commission to commence work on contractual provisions relating to contracts for the supply and construction of large industrial works and contracts on industrial co-operation in general. It was noted that these contracts were of a complex nature and included elements found also in other types of contract. It was thought that these contracts would, therefore, form a basis for possible future work in respect of other related contracts. It was

also felt that the elaboration of model clauses, model contracts or model rules in regard to the supply of large industrial works was a logical sequence to the law of sales.<sup>4</sup>

5. The Commission, therefore, requested the Secretary-General to carry out preparatory work in respect of contracts on the supply and construction of large industrial works and on industrial co-operation.<sup>5</sup> The present study is submitted in compliance with that request.

6. It was generally agreed that the Secretariat in carrying out the preparatory work should have a certain measure of discretion.<sup>6</sup> The Commission endorsed the suggestion by the Secretariat that its work should comprise studies of the available literature and the relevant work of other organizations and should analyse international contract practices. It was noted that the work of the Secretariat would be facilitated if members of the Commission provided the Secretariat with copies of such contracts.<sup>7</sup>

7. The Secretariat is not yet in a position to base its study on an analysis of actual contracts except in a few instances. The collection of contracts in the field of industrialization which the Secretariat has at its disposal is so far too limited to permit substantial conclusions. The Secretariat, however, based its findings on the study of general conditions, model forms of contract and available relevant literature.

## A. Work done by other international organizations

## 1. Conditions and models under study

8. The present study took into account, in particular, the following documents:

(a) General Conditions for the Supply and Erection of Plant and Machinery for Import and Export, No. 188A and 574A prepared by the United Nations Economic Commission for Europe (ECE), referred to as the ECE General Conditions or as ECE 188A/574A;

(b) Guide on Drawing up Contracts for Large Industrial Works (ECE/TRADE/117), referred to as the ECE Guide;

(c) Conditions of Contract (International) for Electrical and Mechanical Works (including Erection on Site)

<sup>4</sup> *Ibid.*, para. 136.

<sup>5</sup> *Ibid.*, para. 143.

<sup>6</sup> *Ibid.*, para. 141.

<sup>7</sup> *Ibid.*, para. 139. By a note-verbale dated 31 October 1980 the Secretary-General solicited the member States of the Commission to provide copies of such contracts and other relevant materials assuring to keep confidential all materials that are of a confidential nature when received. At the time of the preparation of this study, only an industrialized State communicated its willingness to provide the Secretariat with such materials in the near future.

\* 21 April 1981.

<sup>1</sup> A/CN.9/176, para. 31 (Yearbook . . . 1980, part two, V, A).

<sup>2</sup> A/CN.9/191 (Yearbook . . . 1980, part two, V, B).

<sup>3</sup> Report of UNCITRAL on the work of its thirteenth session, *Official Records of the General Assembly, Thirty-fifth Session, Supplement No. 17 (A/35/17)*, para. 143 (Yearbook . . . 1980, part one, II, A).

with Forms of Tender and Agreement prepared by the Fédération Internationale des Ingénieurs-Conseils (FIDIC), second edition 1980, referred to as FIDIC-EMW; and,

(d) Conditions of Contract (International) for Works of Civil Engineering Construction with Forms of Tender and Agreement also prepared by the FIDIC, third edition 1977, referred to as FIDIC-CEC.

9. In addition to those general conditions which are intended for use in international commercial relations, the present study took into account the work of the United Nations Industrial Development Organization (UNIDO) which is engaged in drafting model contracts for the fertilizer industry. The relevant documents are:

(a) Second Draft of the UNIDO Model Form of Turn-key Lump-Sum Contract for the Construction of a Fertilizer Plant (ID/WG.318/1), referred to as UNIDO-TKL;

(b) First Draft of the UNIDO Model Form of the Semi-Turn-key Contract for the Construction of a Fertilizer Plant (ID/WG.318/2), referred to as UNIDO-STC;

(c) Third Draft of the UNIDO Model Form of Cost Reimbursable Contract for the Construction of a Fertilizer Plant (ID/WG.318/3), referred to as UNIDO-CRC;

(d) Consolidated Comments upon the Second Draft of the UNIDO Model Form of Turn-key Contract for the Construction of a Fertilizer Plant (ID/WG.318/4), referred to as comments; and,

(e) Alternative Draft to the Third Draft of the UNIDO Model Form of Cost Reimbursable Contract for the Construction of a Fertilizer Plant (ID/WG.318/5), referred to as counter-proposal.

## 2. Work of UNIDO

10. The Second Consultation Meeting on the Fertilizer Industry at Innsbruck, Austria, 6-10 November 1978, reviewed a Preliminary Draft of the UNIDO Model Form of Cost-Reimbursable Contract for the Construction of a Fertilizer Plant (ID/WG.281/12). This meeting also discussed the preparation of other UNIDO model forms of contract for the construction of a fertilizer plant (ID/WG.281/2).<sup>8</sup>

11. An Expert Group Meeting on UNIDO Model Forms of Contract for Fertilizer Plants was held at Vienna, Austria, 26-30 November 1979. To this meeting the following documents were submitted:

(a) Second Draft of the UNIDO Model Form of Cost Reimbursable Contract for the Construction of a Fertilizer Plant (ID/WG.306/1);

(b) First Draft of the UNIDO Model Form of Turn-key Lump-Sum Contract for the Construction of a Fertilizer Plant (ID/WG.306/2).

12. After that Expert Group Meeting the UNIDO Secretariat prepared further drafts (ID/WG.318/1-3, see paragraph 10, *supra*). Some members of the Expert Group, representatives of contractors from France, Germany, Federal Republic of, Japan, United Kingdom and the United States of America, referred to in this study as an international group of contractors, prepared their consolidated comments upon the Second Draft of the UNIDO Model Form of Turn-key Contract and their Alternative Draft to the UNIDO Model Form of Cost Reimbursable Contract (ID/WG.318/4-5, see paragraph 10, *supra*).

13. These UNIDO documents were submitted to the Third Consultation on the Fertilizer Industry at São Paulo, Brazil, 29 September-2 October 1980, but only part of the UNIDO-TKL model contract was discussed.<sup>9</sup> Therefore, another Expert Group Meeting on Model Contracts for the Construction of a Fertilizer Plant took place at Vienna, Austria, 23 February-6 March 1981, which considered the UNIDO-TKL and UNIDO-CRC models. Another meeting will be held 13-16 April 1981 and it is hoped that these two models will be finalized at the meeting. The UNIDO-STC model and another model on know-how and transfer of technology are expected to be ready by the end of the year.

## 3. Work of ECE

14. The ECE has published several sets of general conditions for contracts on supply and construction of large industrial works.<sup>10</sup> Among them only ECE 188A and 574A, prepared in 1957, have been taken into account, because it was felt that they are representative of approaches undertaken by ECE.

15. The differences between ECE 188A and ECE 574A are marginal. They relate mainly to the formulation of the exonerating circumstances and to the settlement of disputes by arbitration. These differences have their origin in the elaboration of the General Conditions No. 188 by West European countries in 1953 and their later revision in an East-West context in 1955 which led to the adoption of No. 574.

16. The ECE General Conditions relate to a contract which may be called a semi-turn-key contract. They do not relate to any particular branch of industry and are in general oriented on the model of relations between parties from developed countries.

## 4. Work of FIDIC

17. The FIDIC Conditions have been drafted separately for civil engineering works and for electrical and

<sup>8</sup> Report of the Second Consultation Meeting on the Fertilizer Industry (ID/221).

<sup>9</sup> ID/260, paras. 49-56.

<sup>10</sup> See A/CN.9/191, para. 47 (Yearbook . . . 1980, part two, V, B).

mechanical works. The latter relate more or less to all branches of industry. In both cases it is assumed that the purchaser will retain the services of an engineer as his agent, but that the engineer will nevertheless act fairly between the contractor and the purchaser.

18. The FIDIC Conditions are aimed at holding a fair and reasonable balance between the requirements and interests of the parties concerned. The two sets of FIDIC Conditions (see paragraph 8, *supra*) were inadvertently omitted in the study on international contracts in the field of industrial development (see footnote 2, *supra*).

## B. Aim and scope of the study

### 1. Aim of the study

19. The present study aims mainly at identifying legal issues in contracts on the supply and construction of large industrial works (referred to as "works contracts"). For each topic the study attempts to describe the main characteristics, examines and compares the provisions contained in the various forms under study (see paragraphs 8 and 9, *supra*) and comments on them where appropriate.

20. The analysis of the various forms under study is not exhaustive. This is because the purpose of the analysis is not to evaluate existing models as such but to identify legal issues on which the Commission might usefully undertake work without necessarily duplicating the efforts of other organizations. It does not matter, therefore, that the UNIDO model contracts are still in draft form or that all the forms under study have been prepared for different types of contracts, for specific sectors of industry or for an industry in general.

21. It is to be noted that our study proceeds mainly with an examination and comparison of similar provisions on a given issue found in the various forms under study. Of necessity, these provisions have to be isolated from their context. However, no value judgment is intended when comparisons are made as each provision has to be evaluated in its own context. Where a provision appears to favour one party, there might be other provisions which favour the other party. And it has to be borne in mind that all provisions can be more or less counter-balanced by the price.

### 2. Contract on supply and construction of large industrial works: a definition

22. In a previous study the contract on supply and construction of large industrial works has been defined as a "comprehensive contract between the client [the purchaser] and one contractor (supplier) only. This contract comprises all the various aspects of such a

transaction: design, drawings, documentation, delivery, assembly, building, installation, putting into operation, demonstration tests, controls, initial operation of the plant and taking-over. Thus the main characteristic of this contract is its comprehensive nature and complexity."<sup>11</sup>

23. This comprehensive contract, in a pure form, would be a turn-key contract. However, for various economic, financial and technical reasons, not all purchasers favour the turn-key concept.

24. Often, the purchaser participates in the construction of the plant (e.g. in the provision of the necessary connexion for power and water and supply of materials). Very often the purchaser provides all civil engineering work including the construction of buildings; he may also provide the personnel for the assembly, erection, testing and start-up of the plant.<sup>12</sup> Through such participation by the purchaser, the contract becomes a semi-turn-key contract.

25. The purchaser in a turn-key, and more often in a semi-turn-key, situation may make use of a consulting engineer. The involvement of such an engineer, however, does not change the contract into a tripartite transaction: the engineer is acting on behalf of the purchaser.

26. Where the engineer represents the supplier's side, he himself becomes the contractor, who will be responsible for the procurement of all necessary supplies and services. In this situation a cost reimbursable contract will usually be concluded.

27. These are only the main types of contract on supply and construction of large industrial works. Various industries require to a certain extent different approaches (e.g. see part two, XV, *Guaranties*). A chemical plant is different from a rolling mill, and a machine-tool factory is different from a textile mill. The division of labour and the responsibility between the contractor and the purchaser may be different according to their specific purposes.

### 3. Legal nature of a contract on supply and construction of large industrial works

28. While it may not always be easy to distinguish between a contract for work on goods where the contractor also provides the materials and a contract for sale of goods yet to be produced, contracts on supply and construction of large industrial works are clearly distinct from contracts for the sale of goods.<sup>13</sup> Nevertheless, contracts for the supply and construction of large industrial works have some common features with contracts

<sup>11</sup> A/CN.9/191, para. 40 (Yearbook . . . 1980, part two, V, B).

<sup>12</sup> *Ibid.*, para. 42.

<sup>13</sup> *International Encyclopedia of Comparative Law*, vol. VIII, *Specific Contracts*, chapter 8, "Contracts for Work on Goods and Building Contracts" Tübingen, J. C. B. Mohr (Paul Siebeck, 1980), pp. 3 *et seq.*

for sale of goods as a part of the obligation of the contractor is to deliver a plant or equipment.

29. Article 3 of the United Nations Convention on Contracts for the International Sale of Goods, concluded at Vienna in April 1980\* (A/CONF.97/18, hereinafter referred to as Sales Convention), provides that contracts for the supply of goods, to be manufactured or produced, are to be considered sales. There are, however, two important exceptions.

30. The contract is not a sales contract if the party who orders the goods undertakes to supply a substantial part of the materials necessary for such manufacture or production. Except for a pure turn-key contract, in the sphere of manufacture of plants, a supply of materials by the purchaser is quite frequent.

31. The contract is also not a sales contract if the preponderant part of the obligation of the party who furnishes the goods consists in the supply of labour or other services and the "delivery" of the project, the transfer of technology, the erection of the plant, and the putting into operation are supplies of labour and other services.

32. However, the Sales Convention may become applicable in such situations where a contractor and a purchaser conclude a series of separate contracts, e.g. for the supply of equipment, licensing or assembly.

33. Even though the Sales Convention may not be applicable to all works contracts, nonetheless, reference is made to it as it may provide the analogy on how related issues in a works contract may be solved.

34. The study did not, however, look into any national law. It has already been observed that most national legislations do not contain provisions relating specifically to contracts for supply and construction of large industrial works.<sup>14</sup> Most provisions which courts would apply are not of a mandatory nature. As far as mandatory rules are concerned, the Secretariat was unable to obtain them.

#### 4. Scope of study

35. Part two of this study examines clauses which relate to the following:

- I. Drawings and descriptive documents
- II. Supply
- III. Erection
- IV. Passing of risk
- V. Transfer of property
- VI. Transfer of technology
- VII. Quality

#### VIII. Inspection and tests

#### IX. Completion

#### X. Take-over and acceptance

#### XI. Delays and remedies

#### XII. Damages and limitation of liability

#### XIII. Exoneration

#### XIV. Renegotiation

#### XV. Guaranties

#### XVI. Rectification of defects

#### XVII. Termination

#### XVIII. Applicable law

36. The subjects which are not included in part two and on which the Secretariat intends to carry on its preparatory work for the next session of the Working Group are, *inter alia*, the following:

(a) formation of contract; (b) definitions; (c) sub-contractors; (d) assignment; (e) performance bonds; (f) insurance; (g) price calculation; (h) price revision; (i) invoicing; (j) payment conditions; (k) currency and rates of exchange; (l) storage on site; (m) liaison agents; (n) personnel and additional labour; (o) training; (p) taxes and custom duties; (q) settlement of disputes; (r) language of the contract; and, (s) interpretation of the contract.

37. Part three contains some questions which the Working Group may wish to discuss in addition to the general questions for future work as described below.

#### 5. Terms and notions

38. In the various forms under study and also in those contracts in the Secretariat's collection, the names of parties in a works contract have been variously described. Thus, "contractor" is also referred to as "erector", "holder of contract", "client's contracting party", "vendor", "supplier" or "seller" (provided "supplier" and "seller" are not defined in a contract as denoting a third party as in a cost reimbursable contract). "Purchaser" is also referred to as "client", "customer", "buyer" or "employer". However, throughout our study, the parties to a works contract shall be referred to as "contractor" and "purchaser".

#### C. Future work

39. In its suggestion for possible work to be done by UNCITRAL, the previous study suggested the following courses of action open to the Commission: (a) to consider widening the scope of the General Conditions prepared by ECE; (b) to prepare new general conditions; (c) to prepare a model contract form for transactions in the field of industrial plants in general; (d) to deal with

\* Yearbook . . . 1980, part three, I, B.

<sup>14</sup> A/CN.9/191, para. 46 (Yearbook . . . 1980, part two, V, B).



certain specific clauses of such contracts; and (e) to consider the desirability of a draft convention on international contracts for the supply and construction of large industrial works.<sup>15</sup>

40. At the same time, however, it was also suggested that any decision on the direction the work should take and the ultimate end product should be taken in stages on the basis of progress made in the course of preliminary work.<sup>16</sup> This was confirmed by the Commission at its thirteenth session.<sup>17</sup>

41. However, some general direction of work would have to be agreed. In this connexion, in view of the importance given by the Commission to the legal aspects of contracts for the supply and construction of large industrial works, the Working Group might wish to consider whether the preparation of a legal guide in order to assist parties in the negotiation of contracts might be adequate as a preliminary objective.

42. Certainly there are in existence several guides or guidelines such as those prepared by ECE and UNIDO.<sup>18</sup> The ECE Guide, however, addresses itself to enterprises in Europe. Moreover, this Guide is rather brief and general and does not discuss all the legal issues in depth. The various UNIDO documents, on the other hand, deal mainly with economic, technical, administrative and financial aspects of the installation of large industrial works.

43. It appears desirable to have a more comprehensive legal guide which, *inter alia*, identifies the legal issues to be kept in mind when negotiating and drafting contracts on industrial works, describes various approaches pointing out the advantages and disadvantages of each approach and suggests alternative solutions.

44. As work progresses, the contents for inclusion in such a guide may become clearer and a stage may be reached when a model clause approach would be feasible in the context of some clauses. The work may also reveal that a uniform law approach would be appropriate in the light of conflicting national rules as regards other legal issues involved (e.g. in a manner similar to the project currently undertaken by the Working Group on International Contract Practices on liquidated damages and penalty clauses). The examination may further reveal that the preparation of UNCITRAL definitions on some contract terms might be desirable because of the frequent use of legal shorthand in the drafting of contracts—confusion as to their meanings is likely to ensue particularly when parties to an international contract belong to a different legal system or where trade practices differ,

(i.e. a similar consideration which prompted the International Chamber of Commerce to adopt INCOTERMS in order to eliminate such difficulties.<sup>19</sup>

45. The process of identifying the proper formula for end products on distinct legal issues and the implementation may very well progress in parallel with the preparation of guidelines. As the work develops, the scope of each area (e.g. types of contract to be covered) would also become clearer. In fact, such process in stages would be essential in order to attain a meaningful guide designed to contribute to the establishment of a new international economic order in a pragmatic manner. And, only after such processes, a more ambitious approach may become more feasible.<sup>20</sup>

46. Whatever the future decision may be, it appears indispensable first to analyse all relevant issues in depth on each concrete legal issue involved, taking into account the interest of both parties and the need for equitable and balanced solutions. Keeping these considerations in mind, this preliminary study has been prepared to assist the deliberations of the Working Group.<sup>21</sup>

## Part two

### [A/CN.9/WG.V/WP.4/Add.1\*]

#### I. DRAWINGS AND DESCRIPTIVE DOCUMENTS

##### A. Preliminary remarks

1. Throughout the various phases of a contract for the construction of large industrial works, a number of documents are issued by the parties in order to determine the scope of the work to be performed, to follow up on its performance and to enable the purchaser to operate the plant. These documents may consist of catalogues,

\* 26 May 1981.

<sup>19</sup> The ECE General Conditions do not contain a distinct provision on definitions. The FIDIC Conditions and the UNIDO model contract contain many definitions but they are often different from one another.

<sup>20</sup> Since contracts for supply and construction of large industrial works are frequently concluded on the basis of public tenders, it has been suggested that drafting of procurement regulations with contract conditions may be a useful and promising approach for UNCITRAL. As the work progresses to a mature stage, such an undertaking may also become a relatively easy task.

<sup>21</sup> Since a future decision would ultimately have to be taken by the Commission, the Working Group may also wish to note that a report of the Secretary-General (A/CN.9/203) (reproduced in this volume, part two, V, B), which will be before the fourteenth session of the Commission, has discussed, *inter alia*, future courses of action which are open for the Commission.

<sup>15</sup> A/CN.9/191, paras. 52-55 (Yearbook . . . 1980, part two, V, B).

<sup>16</sup> *Ibid.*, para. 148.

<sup>17</sup> Report of the United Nations Commission on International Trade Law on the work of its thirteenth session (A/35/17), para. 141 (Yearbook . . . 1980, part one, II, A).

<sup>18</sup> A/CN.9/191, paras. 48 and 50 (Yearbook . . . 1980, part two, V, B).

prospectuses, circulars, advertisements, illustrated matter, price lists, specifications, drawings, technical documents, programmes and manuals. The time at which the documents are provided by one party to the other and the rights and obligations resulting therefrom will depend on the type of documents.

2. The engineer usually plays a great role in contracts such as those under study. His role is even greater with respect to drawings and descriptive documents. In some cases, the purchaser will be relying entirely on his expertise in this field. Reference to the engineer acting in this capacity can be found mostly in the FIDIC Conditions of contract.

### B. *Types of document and time for submission*

#### 1. *Preliminary documents*

3. The ECE General Conditions contemplate the possibility of documents being submitted by one party to the other in the preliminary stages of the negotiation of the contract. These are usually catalogues, prospectuses, circulars, advertisements, illustrated matter or price lists. Clause 3.1 of both ECE 188A/574A states that "the weights, dimensions, capacities, prices, performance ratings and other data" included in these documents "constitute an approximate guide". These data will bind the parties only if they are "by reference expressly included in the Contract".

#### 2. *Specifications and drawings*

4. In order to award the contract, the purchaser will call for tenders. His call for tenders under the FIDIC Conditions will include not only the general conditions of the contract but also the specifications (clause 1.1 of FIDIC-EMW and 1 (1) (k) of FIDIC-CEC) which often contain drawings (clause 1.1 (p) of FIDIC-EMW and 1 (1) (f) of FIDIC-CEC).

#### 3. *Programme and time schedule*

5. If the specifications and the drawings set out the technical details of the works to be undertaken by the contractor, clause 12.1 of FIDIC-EMW provides that it is the "programme" which is submitted by the contractor that shows "the order of procedure" in which the works are to be carried out, "including the design, manufacture, delivery to Site, erection and commissioning thereof".

6. Clause 12.1 of FIDIC-EMW mentions further that the contractor will also indicate in the "programme":

"... the times by which the Contractor requires the Employer to have obtained any import licences, consents, wayleaves and approvals necessary for the purpose of the Works."

7. Article 12.3 of UNIDO-TKL provides that the time schedule is to be included as an Annexure to the contract. For some of the documents enumerated the approval of the purchaser must be obtained.

8. Once the contract has been awarded, clause 5.1 (a) of FIDIC-EMW requires that the contractor provide "Drawings, samples, patterns and models as may be called for" in the specification or in the programme.

#### 4. *Drawings to be provided by contractor*

9. Under the terms of clause 5.4 of FIDIC-EMW, the contractor must also

"... provide Drawings showing the manner in which the Plant is to be affixed together with all information relating to the Works, required for preparing suitable foundations, for providing suitable access for the Plant and any necessary equipment to the point on Site where the Plant is to be erected and for making all necessary connections to the Plant (whether such connections are to be made by the Contractor under the Contract or not)".

10. A similar provision exists in the ECE General Conditions. Clause 12.1 of both ECE 188A/574A reads:

"The Contractor shall in good time provide drawings showing the manner in which the Plant is to be affixed together with all information relating, unless otherwise agreed, only to the Works, required for preparing suitable foundations, for providing suitable access for the Plant and any necessary equipment to the point on the site where the Plant is to be erected and for making all necessary connexions to the Plant (whether such connexions are to be made by the Contractor under the Contract or not)".

11. Under clause 5.1 (6) of FIDIC-EMW, during the course of the works, the engineer may require the contractor to provide him with "Drawings of the general arrangement and details of the Works". The contractor is obliged to provide him with such drawings. The only case in which he can refuse to comply with the engineer's request is when the engineer requires him to supply copies of shop drawings.

12. Under clause 5.1 of FIDIC-EMW, the drawings and other documents thus submitted must be approved by the engineer. In the event the engineer fails to manifest his approval, there is a presumption that the documents are approved if 28 days have elapsed after their receipt. If the documents are not approved by the engineer, they are to be modified and re-submitted.

13. UNIDO-TKL spells out the delivery procedure of documentation. Articles 2.2.1 and 2.2.2 of Annexure XV of UNIDO-TKL provides as follows:

"2.2.1 The documentation shall be delivered to the PURCHASER's representative in the CONTRAC-

TOR's offices or despatched to the PURCHASER by air-way bill on a freight pre-paid basis and the PURCHASER shall acknowledge each despatch immediately after receiving it. The date of delivery shall be taken to be the date of delivery to the PURCHASER's representative or the date of the air-way bill as the case may be.

"2.2.2 The documentation shall be supplied in six (6) copies and a reproducible copy (with the exclusion of the catalogues, pamphlets and manuals supplied by the Vendors)."

#### 5. Documents to be provided at the end of the works

14. At the end of the works, before they are taken over, other documents have to be provided by the contractor to the purchaser. Under clause 5.6 of FIDIC-EMW, these documents consist of:

"... Operating and Maintenance Instructions together with Drawings (other than shop drawings) of the Works as completed ..."

The reason for providing these drawings is to enable the purchaser to maintain, dismantle, reassemble and adjust all parts of the works.

15. Under clause 5.6 of FIDIC-EMW these documents are deemed to be of such importance that:

"... unless otherwise agreed, the Works shall not be considered to be completed for the purposes of taking over under the terms of Clause 32 (Taking Over) until such instructions and Drawings have been supplied to the Employer."

16. Article 3.1.2 of UNIDO-TKL provides that the contractor is to furnish the purchaser with operational and maintenance manuals. Although article 3.2.6 of UNIDO-TKL provides that "The services relating to Management of Plant Operations, optional Management Assistance and optional Technical Advisory Services ... shall be embodied in appropriate arrangements and agreements ...", article 1 of Annexure XXI enumerates the various manuals which are to be provided by the contractor as part of his contract services, namely operating manual, maintenance manual, manual of safety procedures, manual of analytical procedures, manual for monitoring environmental aspects, manual for instrumentation maintenance, and special instructions for maintenance and calibration of on-line analysers.

17. Furthermore, under article 3 of Annexure XXI of UNIDO-TKL:

"... the CONTRACTOR will provide the PURCHASER in original, all pamphlets, installation, operation and maintenance instructions etc., received from Equipment manufacturers and sub-Contractors of the CONTRACTOR and where required shall

identify the equipment to which such instructions refer."

#### C. Modification or variation

18. Clause 5.2 of FIDIC-EMW states that once the drawings have been approved by the engineer, they are "not [to] be departed from except as provided in Clause 34 (Variations)".

19. It is understandable that, as the works progress, the parties and the engineer may find that the original drawings need to be varied or modified in order to conform to the quality standards imposed by the contract. (See part two, VII, *Quality*.) \* Modifications or variations can also be required because of an error or an omission in the drawings.

20. Clause 12.3 of both ECE 188A/574A state that:

"Any expenses resulting from an error or omission in the drawings or information ... which appears before taking over shall be borne by the Contractor ..."

21. The FIDIC-EMW Conditions contain a similar provision; clause 5.5 states that:

"... any expenses resulting from an error or omission in or from delay in delivery of the Drawings and information ... shall be borne by the Contractor."

22. However, clause 6.1 of FIDIC-EMW provides for an exception to this liability of the contractor as follows:

"The Contractor shall be responsible for any discrepancies, errors or omissions in the Drawings and information supplied by him, whether they have been approved by the Engineer or not, provided that such discrepancies, errors or omissions are not due to incorrect Drawings or inaccurate information furnished to the Contractor in writing by the Employer or the Engineer."

23. Under article 6.3 of FIDIC-EMW, the purchaser is responsible for the "Drawings and information supplied by the Employer or by the Engineer in writing and for the details of special work specified by either of them". Accordingly, article 6.3 of FIDIC-EMW goes on as follows:

"The Employer shall pay to the Contractor for alterations of the work necessitated by reason of incorrect Drawings or information so supplied to the Contractor a sum ascertained and determined in like manner to the valuation of variations under Clause 34 (Variations)."

\* A/CN.9/WG.V/WP.4/Add.2 (reproduced below).

24. The situation with the UNIDO-TKL model differs. In spite of being a turn-key contract, under article 15.1 of UNIDO-TKL the purchaser has full powers "... to direct the CONTRACTOR to alter, amend, omit, change, modify, add to or otherwise vary any of the Works ..."

25. This direction must be given in writing. Once he has been thus directed, the contractor "... shall carry out such work and be bound by the same conditions, so far as applicable, as though the said variations were stated in the Contract and Specifications."

26. Paragraph 2 of article 15 of UNIDO-TKL makes reference to the "PURCHASER/Engineer". This would seem to indicate that the purchaser may retain the services of an engineer or that an engineer is closely involved with the project and that his decision or his instructions are considered as being those of the purchaser.

27. Under article 15.3 of UNIDO-TKL, if the changes requested by the purchaser are solely due to "defects, omissions or errors in the Plant(s) or Work(s)", resulting from "any discrepancies or mistakes in design, process, engineering, instructions, specifications, inspections, procurement, fabrication and supply, civil engineering, erection, and errors and/or omissions (as the case may be)", the contractor will have to bear their costs.

28. On the other hand, article 15.2 of UNIDO-TKL provides that if the changes requested by the purchaser do not result from such defects, omissions or errors, the difference in cost is to be added to or deducted from the contract price, the engineer intervening in the assessment of the difference. In the event that no agreement is reached by the parties, reference is made to the provisions of the contract concerning settlement of disputes and arbitration.

29. Under article 15.4 of UNIDO-TKL, variations can also be initiated by the contractor if he "is of the opinion that such variation is necessary to correct any defect in the Works which has occurred or which would otherwise occur ..."

30. In such an event, the contractor is not allowed any extra costs under article 15.5 of UNIDO-TKL "... even if such changes or variations are as a result of changes in detailed project schedule created by change in material deliveries, and/or incidental to time changes related to mechanical completion, or due to changes in piping layout or design performed by the CONTRACTOR as a result of detailed engineering."

31. The procedure to be followed to vary or modify the drawings varies from one type of contract to another. Needless to say, in contracts where an engineer is closely involved, he will have a great role to play in these matters.

32. Under the FIDIC Conditions the procedure to be followed to modify the drawings varies slightly from one set of conditions to the other. However, as a rule, it can be said that nothing can be modified or varied without the written permission of the engineer.

33. Under clause 34.1 of FIDIC-EMW, the engineer must give the contractor reasonable notice of the variations to be undertaken, so that the contractor can make the necessary arrangements. The same article provides that once the contractor has been advised of the variations to be made, he "shall carry out such variations and be bound by the same conditions, so far as applicable ..."

34. Article 15.6 of UNIDO-TKL provides that in the event that the modifications are initiated by the contractor, the purchaser must approve them. However, in view of the nature of the contract, the article provides further that:

"The PURCHASER shall not refuse to approve any variation which is necessary to correct any defect in the Works which has occurred or which would otherwise occur if the CONTRACTOR's proposal is not accepted, or if any modifications or rectifications are required ... In all other cases, the PURCHASER may give or refuse his approval as he thinks fit and his decision shall be final."

35. It may happen that modifications or variations which are required by the purchaser are of such a nature as to prevent the contractor "from fulfilling any of his obligations under the contract". In such a case, article 15.8 of UNIDO-TKL provides that the contractor:

"... shall notify the PURCHASER thereto in writing and the PURCHASER shall decide forthwith whether or not the same shall be carried out. If the PURCHASER re-confirms in writing his intention to carry out the variations, then the said obligations of the CONTRACTOR shall be modified to such an extent as may be justified ..."

36. Under article 15.12 of UNIDO-TKL, once the purchaser has approved the modifications, they are to be embodied in a change order to be signed by the parties or their authorized representatives, and:

"... such Change Orders shall be deemed to form part of the Contract and subject to all of the terms and conditions therein, unless otherwise excepted."

37. Article 15.10 of UNIDO-TKL provides that in the event of a dispute as to whether the variations are within the contractual obligations of the contractor it shall be decided by a neutral party. The same article also provides that if the purchaser considers that the services to be rendered as a result of such variations are exorbitant, the quantum of payment shall also be decided by the neutral party. And, pending his decision, the contractor has to proceed without delay to effect the changes.

### D. Ownership of the documents

38. On account of the nature of some of the information contained in the drawings and documents submitted by one party to the other, some of the forms under study contain provisions dealing with the ownership of the documents.

39. Clauses 3.2 and 3.3 of both ECE 188A/574A provide that the "drawings or technical documents intended for use in the construction or erection of the Works or of part thereof" and submitted by one party to the other (purchaser to contractor or vice versa) remain "the exclusive property" of the party who furnished them.

40. This restriction has the effect of imposing on the party receiving the documents an obligation as to confidentiality. This is why clauses 3.2 and 3.3 of both ECE 188A/574A state that he cannot copy, reproduce, transmit or communicate them to a third party without the other party's consent.

41. In the case of the documents provided by the contractor to the purchaser, an exception is provided for by article 3.2 of both ECE 188A/574A which states:

"the said plans and documents shall be the property of the Purchaser:

"(a) If it is expressly so agreed, or

"(b) If they are referable to a separate preliminary development contract on which no actual construction was to be performed and in which the property of the Contractor in the said plans and documents was not reserved."

42. As for the documents to be provided by the contractor at the commencement of the guaranty period, clause 3.4 of both ECE 188A/574A provides that they become the property of the purchaser without any restriction. However, the contractor may stipulate that they should remain confidential.

43. The other forms under study do not contain any such provisions. However, it goes without saying that the documents dealing with matters related to transfer of technology partake of the obligation as to confidentiality imposed to the parties in this respect. (See part two, VI, *Transfer of Technology*.)\*

## II. SUPPLY

### A. General remarks

44. The items which the contractor has to supply in order to commence erection of the works are varied and

numerous and include machinery, materials, erection equipment, labour, utilities and temporary and ancillary works. In this chapter we will examine only the parties' obligations for the supply, transportation and storage of the machinery and materials; the materials may be intended for incorporation into the permanent works or they may be required for purposes of construction only. (For a discussion of the supply of erection equipment and labour, see III, *Erection of Works, infra*.)

45. The type of contractual provisions relating to the supply of the machinery and the necessary materials will depend to a large extent on the type of contract and the actual content of the work to be performed under the contract. A full turn-key contract normally covers the supply by the contractor of the design for the plant, the machinery, technical documentation and the necessary materials.

### B. Parties' obligations

#### 1. Obligation to supply

46. In a works contract, the contractor's obligation to erect and complete the described work implies an undertaking on his part to do any work and supply materials which are necessary to complete the work in accordance with the contract. Under FIDIC-CEC, this special obligation of the contractor is expressly stated. Clause 8 (1) states:

"The Contractor shall, subject to the provisions of the Contract, and with due care and diligence . . . provide all labour, including the supervision thereof, materials, Constructional Plant and all other things, whether of a temporary or permanent nature, required in and for such execution and maintenance, so far as the necessity for providing the same is specified in or is reasonably to be inferred from the Contract."

47. Under FIDIC-EMW, only the contractor's obligation to supply labour and contractor's equipment is stated. The responsibility for the supply of the machinery and the necessary materials is left to the parties' agreement. Clause 7.1 provides:

"The Contractor shall, subject to the provisions of the Contract . . . provide all labour, including the supervision thereof, and Contractor's Equipment, necessary therefor and for carrying out his obligations . . . so far as the necessity for providing the same is specified in or is reasonably to be inferred from the Contract."

48. Under the UNIDO model contracts the contractor is also responsible for the supply of machinery and materials. It is always in the interests of the purchaser to have the machinery and materials described and, if necessary, approved by the purchaser; to this end under the UNIDO models the contractor is required to

\* A/CN.9/WG.V/WP.4/Add.2 (reproduced below).

provide the purchaser with an itemized list of the machinery and materials to be supplied under the contract. Article 4.9 of UNIDO-TKL states:

"The CONTRACTOR shall be responsible for the supply of the complete plant and equipment . . . The list of the Plant and Equipment as well as other Materials . . . shall represent the complete Plant . . ."

49. The contractor's obligation is, however, not limited to the supply of specified items; he is required to supply also materials which are required for the work. Article 4.9 of UNIDO-TKL states:

". . . Any additional item(s) required but not specified . . . shall be supplied by the CONTRACTOR. Notwithstanding anything to the contrary expressed in the Contract, the CONTRACTOR shall supply a complete Turn-key Plant . . . together with all the specified off-sites and utilities . . ."

50. Under UNIDO-CRC the contractor procures the materials on the purchaser's account. The extent of his obligations is, however, the same. Article 4.12 provides:

"The CONTRACTOR will procure all plant and equipment, material and spare parts on behalf of the PURCHASER . . . Notwithstanding the fact that the ultimate purchase is to be made on the PURCHASER's account, the CONTRACTOR shall be obligated to ensure that all procurement is accomplished so as to enable the Plant to meet the objectives expressed in Article 2, subject to the PURCHASER carrying out his obligations. The procurement shall be carried out by the CONTRACTOR in such manner that the Plant is capable of meeting the Performance Guarantees . . . The CONTRACTOR shall also assist the PURCHASER to obtain remedial action from Vendors (where such is necessary) and the CONTRACTOR's services for any required procurement and/or inspection shall be discharged free of additional costs to the PURCHASER . . ."

51. UNIDO-STC is explicit on the contractor's responsibility to supply necessary materials that are not described in the contract. Article 4.8 states:

". . . however if any equipment not specified in this Contract is required to complete the Plant . . . these shall form part of the CONTRACTOR's supply pursuant to this Contract and shall be supplied FOB without additional cost or expense to the PURCHASER within the agreed lump sum price . . ."

52. Under the ECE General Conditions, there are provisions for shared responsibility with respect to the provision of plant, materials and other facilities connected with the work. The contractor is responsible for the supply of the plant, materials and the constructional equipment. The purchaser assumes responsibility for most of the pre-construction work including the supply of services and utilities necessary for the implementation

of the contract. Clause 6.1 of both ECE 188A/574A provides:

"The price shall be on the understanding that the following conditions are fulfilled, except so far as the Purchaser has informed the Contractor to the contrary:

". . .

"(c) Such equipment, consumable stores, water and power as are specified in the Contract shall be available to the Contractor on the site in good time, and, unless otherwise agreed, free of charge to the Contractor;

"(d) The Purchaser shall provide the Contractor (free of charge, unless otherwise agreed) with closed or guarded premises on or near the site as a protection against theft and deterioration of the Plant to be erected, of the tools and equipment required therefor, and of the clothing of the Contractor's employees . . ."

## 2. *Obligation to transport materials*

53. In a turn-key lump-sum contract, the contractor's responsibility is not divided up in terms of the various activities. The contractor is responsible for the supply and transport of the materials and the contract price under a turn-key contract includes the cost of transporting the machinery and the materials. In other types of contract transportation costs may be separately charged. Some of the forms analysed are not explicit on the parties' responsibility for transporting the machinery and materials. Sometimes the responsibility is stated only by implication.

54. Under FIDIC-CEC and FIDIC-EMW, the contractor is obliged to make his own arrangements for the transport of the plant and materials at his own cost since under clause 70.(1) of FIDIC-CEC and clause 52.1 of FIDIC-EMW transport costs are included in the contract price.

55. Under UNIDO-TKL and UNIDO-STC, responsibility for the transportation of the equipment is expressly stipulated. Article 4.13 of UNIDO-TKL states:

"The CONTRACTOR shall be responsible for the transportation of equipment from the port of despatch FOB to the receipt CIF entry port in the PURCHASER's country and onward despatch to the Site."

56. Under UNIDO-CRC the contractor is not directly responsible for the transportation of the plant and materials. He is, however, obliged to assist the purchaser in ensuring that the manufacturers expedite the supply and transport of the necessary equipment. Article 4.14 states:

"The CONTRACTOR shall . . . be obligated to require the proper carrying out by the Vendors of all packaging and the expediting of necessary transportation FOB to the point of despatch."

57. Under the ECE General Conditions, it is contemplated that the purchaser may be responsible for the preparatory work and the transport of the materials and equipment. Clause 12.2 of both ECE 188A/574A states:

"The preparatory work shall be executed by the Purchaser in accordance with the drawings and information provided by the Contractor . . . It shall be completed in good time and the foundations shall be capable of taking the Plant at the proper time. Where the Purchaser is responsible for transporting the Plant, it shall be on the Site in good time."

### 3. *Obligation to take care of machinery and materials during transportation*

58. The contractor's responsibility for transporting the machinery and materials subsumes the obligation to pack and mark the materials to ensure their safety during normal transportation. As indicated in paragraph 53 under a turn-key contract the cost of packing will be included in the contract price. Article 4 of both ECE 188A/574A states:

"Unless otherwise specified:

". . .

"(b) Prices quoted in tenders and in the Contract shall include the cost of packing or protection required under normal transport conditions to prevent damage to or deterioration of the Plant before it reaches its destination as stated in the Contract."

59. UNIDO-TKL has very elaborate provisions stating the contractor's obligations for the marking, packing and despatch of the materials. Article 12.2.1 states:

"All goods shall be marked and the invoices prepared in accordance with the instructions of the PURCHASER . . ."

60. Transportation of the machinery may require observance of local rules in the purchaser's country. Under the UNIDO-TKL, the purchaser is required to assist the contractor in obtaining the necessary permits. Article 12.2.7 states:

"The CONTRACTOR acknowledges its familiarity with facilities at the harbours (both in the manufacturer's and PURCHASER's country) and between the harbour and Site. The CONTRACTOR shall be responsible for the packing and delivery of the equipment (packed in proper dimensions as to size) in such manner that the equipment arrives at Site for erection, within the Contractual time schedules. The CONTRACTOR shall be responsible for obtaining any road or rail permits required for the purposes, but the PURCHASER shall assist the CONTRACTOR in obtaining such permits."

### 4. *Obligation to provide for storage of materials at site*

61. The extent of the contractor's obligation for the safe storage of the materials will again depend on the type of contract. In a turn-key contract care and adequate storage of the machinery and materials of the contractor will be the responsibility of the contractor.

62. Under UNIDO-TKL the adequate storage of the machinery is the responsibility of the contractor. Article 12.4 states:

"The CONTRACTOR shall be obliged to arrange for and have ready adequate warehouse facilities at the Site to receive packages. In the event that permanent facilities are not ready or available, the CONTRACTOR shall provide sufficiently adequate temporary facilities at his cost in good time at the Site, to the satisfaction of the PURCHASER. Notwithstanding the requirement for the marking of packages . . . the instructions of the Engineer as regards storage shall be adhered to in the event that additional storage protection is required."

63. The ECE General Conditions anticipate that the purchaser may be responsible for the storage of the materials. Article 6.1 of both ECE 188A/574A states:

"The price shall be on the understanding that the following conditions are fulfilled, except so far as the Purchaser has informed the Contractor to the contrary:

". . .

"(e) The Contractor shall not be required to . . . take any . . . measures to enable the Plant to be brought from the point where it has been unloaded to the point on the site where it is to be erected, unless the Contractor has agreed to deliver the Plant to the last mentioned point.

"Any departure from the conditions mentioned in this paragraph shall attract an extra charge."

### C. *Time for delivery*

64. The time for delivery will depend on the nature of each work. In some of the forms under study we find general provisions requiring the contractor to make "timely" or "expeditious" delivery.

65. Article 14 of UNIDO-TKL, for example, states:

"14.15 The CONTRACTOR shall ensure that the despatch and delivery of plant and equipment are expeditiously implemented and efficiently co-ordinated . . . in complete accordance with the terms, conditions and procedures for delivery in this Contract and/or also as may be contained in any Purchase Orders to Vendors."



"14.16 The CONTRACTOR shall take all necessary measures to ensure that all export licences (if necessary) and shipping documentation are arranged and issued in a timely manner."

### III. ERECTION

#### A. Introduction

66. The nature and extent of the obligations and responsibilities of the parties to erect a plant, machinery or other equipment depend largely on two factors: first, on the types of works contract, e.g. whether it is a turn-key or semi-turn-key contract; secondly, on the kinds of plant to be erected. The construction of a steel rolling mill is very different from that of a fertilizer plant.

67. The nature of the various forms under study must be borne in mind when considering the question of erection (see part one, *Introduction*).\* Only the main obligations and responsibilities of the contractor, the engineer and the purchaser in regard to erection are discussed here.

#### B. Obligations and responsibilities of contractor, engineer and purchaser

##### 1. Erection of plant

###### (a) Turn-key lump-sum contract: UNIDO-TKL

68. To illustrate the main differences in the obligations and responsibilities of the contractor and the purchaser in regard to the erection of a plant in a turn-key lump-sum contract and in a semi-turn-key contract, the UNIDO-TKL and the UNIDO-STC model contracts will be considered.

69. In the UNIDO turn-key lump-sum contract for the construction of a fertilizer plant (UNIDO-TKL), the contractor undertakes to erect all plant and equipment within the contractual terms (article 3.2.5). This in effect includes the overall work required for the establishment of the plant until its successful operation according to the specifications laid down in the contract (article 3.1). This responsibility is contained in a number of provisions. For example, article 4.9 reads:

"The CONTRACTOR shall be responsible for the supply of the complete plant and equipment in accordance with Article 12 and as expressed elsewhere in this Contract . . . the CONTRACTOR shall supply a complete Turn-Key Plant for the production of (1,000) tons per day ammonia and (1,725) tons per day urea, . . ."

70. The responsibilities of the contractor for the erection of the plant and equipment under article 12.7 include:

"12.7.1.1: Erection of all equipment in place.

"12.7.1.2: Erection of all steel structures, walkways, gangways, stairs, platforms, etc.

"12.7.1.3: Assembly and welding of all piping, fittings, etc. both above and below the ground.

"12.7.1.4: Assembly and erection of instrumentation, panel control boards and all interconnecting wiring, piping and equipment.

"12.7.1.5: Installation of all electrical equipment, and connection of all cables, starters and all other equipment.

"12.7.1.6: Installing of all utility equipment, and connecting such equipment.

"12.7.1.7: Insulation of all equipment where required (including supply of insulation).

"12.7.1.8: Painting of all equipment (including supply of paint).

"12.7.1.9: Installation of all workshop, laboratory and office equipment, including air conditioning equipment and telephone facilities.

"12.7.1.10: Installation and erection of all waste treatment and sewerage facilities.

"12.7.1.11: Installation of all safety and warning devices.

"12.7.1.12: All or any other erection work that may be required to complete the Plant, other than the exclusions contained in . . .

"12.7.1.12.1: The erection of the plant and equipment shall conform with the details . . ."

71. The contractor must ensure that all supply, construction and erection is undertaken so as to enable the plant to meet its objectives set out in the contract (article 4.10).

###### (b) Semi-turn-key contract: UNIDO-STC

72. Being a semi-turn-key contract, the establishment of the plant may not reside in the contractor, for the purchaser is given the option to appoint another party to erect the plant. Article 3.2.18 reads:

"The Plant shall be erected (article 3.1.15) by the CONTRACTOR or by such other party appointed by the PURCHASER (provided that such other party is not a competitor of the CONTRACTOR), under the technical direction and supervision of the CONTRACTOR's personnel."

73. Thus the contractor's role in the erection of the plant would be only that of a supervisor, should the purchaser appoint another person to erect the plant. The

\* A/CN.9/WG.V/WP.4 (reproduced above).

main supervisory responsibilities of the contractor under article 13.5.1 include:

"The CONTRACTOR shall be responsible for giving technical direction and *supervising* the erection of all the plant and equipment . . . Without limiting the generality of the foregoing, these *supervisory services* shall cover, (but shall not be limited to):

"13.5.1.1: Erection of all equipment in place.

"13.5.1.2: Erection of all steel structures, walkways, gangways, stairs, platforms, etc.

"13.5.1.3: Assembly and welding of all piping, fittings, etc. both above and below the ground.

"13.5.1.4: Assembly and erection of instrumentation, panel control boards and all interconnecting wiring, piping and equipment.

"13.5.1.5: Installation of all electrical equipment, and connection of all cables, starters and all other equipment.

"13.5.1.6: Installing of all utility equipment, and connecting such equipment.

"13.5.1.7: Insulation of all equipment where required (including supply of insulation).

"13.5.1.8: Painting of all equipment (including supply of paint)."

74. Other aspects of supervision relate to the installation of certain equipment and facilities necessary for the erection of the plant.

## 2. Materials for erection of plant

75. The materials for the erection of the plant, sometimes referred to as the "contractor's equipment", must be distinguished from the "equipment" that is to be erected. The distinction between the two is made in the UNIDO-model contracts and in the FIDIC-EMW Conditions. "CONTRACTOR's equipment" is defined, for example, in UNIDO-TKL as "... any equipment, sheds, materials, tools, stores or things brought on Site by or on behalf of the CONTRACTOR for the execution of the Contract, but not for permanent incorporation in the Plant" (article 1.11). On the other hand, "equipment" is defined as "all of the equipment, machinery, materials . . . required to be incorporated permanently into the Plant(s) (with the exclusion of materials for civil works) in order for the Plant to be built in accordance with the Contract" (article 1.17).

76. Under article 4.9 of the UNIDO-TKL model contract, the contractor must establish a "more complete list of equipment and materials to be procured" within four months from the effective date of the contract for the approval of the purchaser.

77. It is generally the responsibility of the contractor, at least in a turn-key contract, to provide all erection

materials and contractor's equipment. Article 4.22 of the UNIDO-TKL model contract states that the contractor is to provide "all erection equipment and materials for the erection and installation of the Plant". And article 12.7.2 expressly mentions some of this equipment:

"The CONTRACTOR shall supply all materials needed for the erection and installation of the Works, all tools, tackles, cranes and other erection equipment required, and shall provide all instruments required for the proper erection and testing of the Works."

78. Under the UNIDO-STC model contract, the contractor is also required, within four months after the effective date of the contract, to provide a list of erection equipment and materials to the purchaser. The materials are to be supplied by the contractor (article 1.10).

79. Similarly, in the FIDIC-EMW Conditions the contractor must provide, at his own expense, all "contractor's equipment", haulage and power necessary to execute and complete the works (clause 14.1).

80. However, if the purchaser has certain equipment on his site, the contractor may use these but he has to pay a reasonable sum for its use. The FIDIC-EMW Conditions contemplate such a situation:

*Clause 14.4:* "The Employer shall at the request of the Contractor and for the execution of the Works operate any suitable lifting equipment belonging to the Employer that may be available on the Site and of which details are given in Part II of these Conditions and the Contractor shall pay a reasonable sum therefor. The Employer shall during such operation retain control of and be responsible for the safe working of the lifting equipment but shall not be responsible for any negligence of the Contractor."

## 3. Preparatory work

81. It is beyond the scope of this chapter to deal with the construction of various infrastructure such as the construction of road or rail within the battery limits of the plant. But certain preparatory work immediately connected with erection should be mentioned.

82. Thus, for example, in the FIDIC-EMW Conditions, the contractor must submit to the engineer for his approval a programme showing the order of procedure in which he proposes to carry out the works including the design, manufacture, delivery to site, erection and commissioning thereof. The programme must also indicate the times by which the contractor requires the purchaser to have obtained any import licences, consents, wayleaves and approvals necessary for the purpose of the works (clause 12.1).

83. The ECE188A/574A General Conditions provide an example of the position in a semi-turn-key contract where the purchaser has to execute the preparatory work in accordance with the drawings and

information provided by the contractor. Clause 12.2 of both the ECE General Conditions provides that the preparatory work must be completed in good time and the foundations must be capable of taking the plant at the proper time. And, where the purchaser is responsible for transporting the plant, it must be on the site in good time.

#### 4. Supervision of work

##### (a) UNIDO-TKL

84. The expression "supervision" includes "direction and responsibility for the activities or matters or work or procedures being the subject of supervision and management . . . of all the Works until Provisional Acceptance" (article 13.8).

85. The contractor is charged with the responsibility for the supervision of all work at site until provisional acceptance of the works (article 13.1). He must provide an adequate number of suitability qualified and experienced personnel. The supervisory services under Article 13 include:

"13.1.1: Supervision and management of transportation equipment.

"13.1.2: Supervision and management of construction and erection equipment.

"13.1.3: Supervision and management of the civil works.

"13.1.4: Supervision and management of erection.

"13.1.5: Supervision and management of stores and warehouse management.

"13.1.6: Supervision and management of all tests.

"13.1.7: Supervision and management of pre-commissioning and start-up operations.

"13.1.8: Supervision and management of the entire Works until Provisional Acceptance."

86. After the plant has started-up the contractor has to supervise the operation until the guarantee tests are satisfactorily completed.

##### (b) UNIDO-STC

87. The provision on supervision in UNIDO-STC contemplates a situation where the purchaser appoints another party to erect the plant (see paragraphs 72 and 73 *supra*). The contractor's role is then confined mainly to that of a project supervisor. The purchaser himself may undertake the erection. Article 13.1.1 speaks of "supervision of the equipment manufactured by or on behalf of the PURCHASER which is to be undertaken by the contractor. Other aspects of supervision laid down in article 13 include:

"13.1.2: Supervision of erection and installation of erection equipment.

"13.1.3: Supervision of stores and warehouse.

"13.1.4: Supervision of pre-commissioning tests and start-up operations.

"13.1.5: Supervision and demonstration of performance guarantee tests."

88. It is noted that, unlike UNIDO-TKL, the supervision does not include management. (See paragraph 85 *supra*.)

89. As noted in paragraph 73 *supra*, if the purchaser appoints another to erect the plant, the supervision by the contractor will extend to all aspects of erection set out in article 13.5.1.

90. Where the contractor's role is limited to that of supervision, he is responsible for the following matters during erection:

##### "Article 13.6

"The CONTRACTOR shall be responsible *inter alia* during the erection for the following:

"13.6.1: For correctness and competency of the instructions given by him or his Chief Engineer.

"13.6.2: For securing that the units be erected and connected, if necessary, according to requirements of the technical documents drafted by the CONTRACTOR or further instructions regarding modifications, corrections and other kinds of alterations as the case may be.

"13.6.3: For technically checking the erection works, to reveal erection faults, if any. The CONTRACTOR shall issue suitable and workmanlike instructions to remove such defects.

"13.6.4: For checking compliance with the instructions issued by him. If any deficiencies are found, the Chief Engineer shall enter the deficiencies during the execution in the erection journal of the relevant unit and suggest remedies."

##### (c) FIDIC-EMW

91. In the FIDIC-EMW Conditions, the contractor is under an obligation to employ competent representatives to supervise or superintend the carrying out of the works. Clause 13.1 provides:

"The Contractor shall employ one or more competent representatives whose name or names shall have previously been communicated in writing to the Engineer by the Contractor, to superintend the carrying out of the Works on the Site. The said representative, or if more than one shall be employed, then one of such representatives, shall be present on the Site during all working hours, and any orders or instructions which the Engineer may give to the said representative of the Contractor shall be deemed to have been given to the Contractor."

92. Clause 13.2 reads:

"The Engineer shall be at liberty by notice in writing to the Contractor to object to any representative or person employed by the Contractor in the execution of or otherwise about the Works who shall, in the opinion of the Engineer, misconduct himself or be incompetent or negligent, and the Contractor shall remove such person from the Works."

## 5. Access to works

93. Access to the works by the contractor, the engineer and the purchaser is very important as it enables them to execute, supervise and/or manage the erection properly. Hence provisions for access are contained in all works contracts.

### (a) Contractor's obligation

94. The contractor must permit the engineer to have access to the works at all times during the tenure of the contract. (See UNIDO-TKL article 13.6 and UNIDO-STC article 13.11.)

95. The contractor must afford every facility for access to any place where work is being undertaken and must give every assistance in obtaining the right for such access in connexion with the execution of the work under the contract (UNIDO-TKL article 13.9 and UNIDO-STC article 13.11).

96. Similarly, the contractor in FIDIC-EMW must permit reasonable access to the works to the employees of the purchaser. Clause 14.5 reads:

"The Contractor shall, in accordance with the requirements of the Engineer, afford all reasonable opportunities for carrying out their work to any other contractors employed by the Employer and their workmen and the workmen of the Employer and of any other duly constituted authorities who may be employed in the execution on or near the Site of any work not included in the Contract or of any contract which the Employer may enter into in connection with or ancillary to the Works."

### (b) Purchaser's obligation

97. The purchaser has to afford the contractor access to the works and site. Thus, for example, article 13.10 of the UNIDO-TKL provides that "the PURCHASER shall afford every facility and assistance in . . . the right of access to . . . Site, workshops or persons within (PURCHASER's country) as is required in connexion with [the] Contract."

98. Article 13.11 of the UNIDO-TKL further provides that the contractor and his authorized personnel shall have free access to the site of the works, storage yards, fabrication sheds, utilities and laboratories set up or intended for use for setting up the works under the

contract. The contractor shall have exclusive access to the areas of the site where he is working.

99. In the UNIDO model contracts (e.g. TKL and STC), the purchaser must provide the necessary assistance in obtaining permission from his Government for visits/stay and travel of the contractor or his authorized personnel (UNIDO-TKL article 13.11; UNIDO-STC article 13.13).

100. After provisional acceptance the purchaser must allow the contractor to visit the works in operation for a period of three (3) years for the purpose of examining its operation, etc. However, the purchaser may exclude the nationals of certain countries from visiting the plant and/or the site (UNIDO-TKL article 13.12; UNIDO-STC article 13.14).

101. In FIDIC-EMW, where the contractor is employed to execute the works for the purchaser, the following obligations are imposed on the purchaser regarding access:

### *Access to and possession of the site*

Clause 20.1: "Subject to Sub-Clause 4 of this Clause access to and possession of the Site shall be afforded to the Contractor by the Employer in reasonable time and, except in so far as the Contract may provide to the contrary, the Employer shall provide a road or railway suitable for the transport of all Plant and Contractor's Equipment necessary for the execution of the Works from an adequate public thoroughfare or railway available to the Contractor to the point on the Site where it is to be delivered or used."

### *Foundations*

Clause 20.2: "If a building structure foundation or approach is by the Contract to be provided by the Employer such building structure foundation or approach shall be in a condition suitable for the efficient transport, reception, installation and maintenance of the Works."

### *Authority for access*

Clause 20.3: "In the execution of the Works no persons other than the Contractor, sub-Contractors and his and their employees shall be allowed on the Site except by the written permission of the Engineer but facilities to inspect the Works at all times shall be afforded to the Engineer and his representatives and other authorities, officials, or representatives of the Employer."

### *Access not exclusive*

Clause 20.4: "The access to and possession of the Site referred to in Sub-Clause 1 hereof shall not be exclusive to the Contractor but only such as shall enable him to execute the Works."

102. Clause 18 of both ECE 188A/574A provides that until the works are taken over and during any works resulting from the operation of the guaranty, the contractor has the right at any time during the hours of work on the site to inspect the works at his own expense. In proceeding to the site, the inspectors must observe the regulations as to movement in force at the purchaser's premises.

(c) *Access by third parties*

103. Where in the opinion of the engineer (acting on behalf of the purchaser) it is necessary that third parties, e.g. additional contractors, have access to the work the contractor must allow such access. However, such third parties must not be direct competitors of the contractor (UNIDO-TKL article 13.[14].1).

104. Where the contractor has incurred expenses in complying with the above article 13.14.1 in respect of such third parties, the purchaser must pay to the contractor the cost of any services provided by the contractor (UNIDO-TKL article 13.14.2).

6. *Labour and working conditions*

105. The question of labour and "working conditions" depends on the types of works contract, the kinds of plant to be erected and the price. For example, in a turn-key lump-sum contract the contractor is responsible for erection of a plant up to the point when the key is ready to be turned. The contract price for the plant includes the execution of the contract, the performance of the contractor's services and the completion of works. Hence, the contractor himself is generally responsible for the labour and all aspects in connexion with it, and there is no necessity of having detailed provisions pertaining to labour.

106. Bearing in mind that the ECE 188A/574A General Conditions are geared to semi-turn-key contracts, it is to be noted that in clause 14.1 of both the General Conditions "if the Contractor so requires in good time the Purchaser shall make available to the Contractor free of charge such skilled and unskilled labour as is provided for in the contract and such further reasonable amount of unskilled labour as may be found to be necessary even if not provided for in the Contract."

107. Working conditions bear upon the question of price. For example, clause 6.1 of both ECE 188A/574A provides:

"The price shall be on the understanding that the following conditions are fulfilled, except so far as the Purchaser has informed the Contractor to the contrary:

"(a) The works shall not be carried out in unhealthy or dangerous surroundings;

"(b) The Contractor's employees shall be able to

obtain suitable and convenient board and lodging in the neighbourhood of the site and shall have access to adequate medical services;

"(c) Such equipment, consumable stores, water and power as are specified in the Contract shall be available to the Contractor on the site in good time, and, unless otherwise agreed, free of charge to the Contractor;

"(d) The Purchaser shall provide the Contractor (free of charge, unless otherwise agreed) with closed or guarded premises on or near the site as a protection against theft and deterioration of the Plant to be erected, of the tools and equipment required therefor, and of the clothing of the Contractor's employees;

"(e) The Contractor shall not be required to undertake any works of construction or demolition or to take any other unusual measures to enable the Plant to be brought from the point where it has been unloaded to the point on the site where it is to be erected, unless the Contractor has agreed to deliver the Plant to the last mentioned point.

"Any departure from the conditions mentioned in this paragraph shall attract an extra charge."

And, clause 6.2 provides that:

"If the circumstances resulting from such departure are such that it would be unreasonable to require the Contractor to proceed with the Works, the Contractor may, without prejudice to his rights under the Contract, refuse to do so."

108. Other aspects of labour dealt with in both the ECE General Conditions are:

*Overtime*

*Clause 16.1:* "Any overtime and the conditions thereof shall, within the limits of the laws and regulations of the Contractor's country and of the country where erection is carried out, be as agreed between the parties."

*Work outside the contract*

*Clause 17.1:* "The Purchaser shall not be entitled to use the Contractor's employees on any work unconnected with the subject-matter of the Contract without the previous consent of the Contractor. Where the Contractor so consents, he shall not be under any liability in respect of such work, and the Purchaser shall be responsible for the safety of the Contractor's employees while employed on such work."

*Safety regulations*

*Clause 15.1:* "The Purchaser shall notify the Contractor in full of the safety regulations which the Purchaser imposes on his own employees and the Contractor shall secure the observance by his employees of such safety regulations."

"15.2: If breaches of these regulations come to the notice of the Purchaser, he must inform the Contractor in writing forthwith, and may forbid persons guilty of such breaches entry to the site.

"15.3: The Contractor shall inform the Purchaser in full of any special dangers which the execution of the Works may entail."

109. In the FIDIC-EMW Conditions it is expressly provided that the contractor has to make his own arrangements for the engagement of all labour, local or otherwise, and to pay for their expenses such as transport and housing. Provision is also made in regard to the supply of utilities to the contractor's employees. Other provisions deal with the responsibility of the contractor for his sub-contractors, agents and employees in respect of certain matters such as the sale or importation of alcoholic liquor or drugs, sale of arms and ammunition, and disorderly conduct (see clause 22). Even in the absence of express provisions in a contract, most of these matters would be governed by the law of the place where the works are carried out.

#### 7. Miscellaneous

110. The ECE188A/574A General Conditions attempt to list certain items which are to be separately charged when erection is either on a "time basis" or when it is a "lump-sum erection".

*Clause 7. "Erection on a Time Basis and Lump-sum Erection"*

"7.1 When erection is carried out on a time basis the following items shall be separately charged:

"(a) All travelling expenses incurred by the Contractor in respect of his employees and the transport of their equipment and personal effects (within reasonable limits) in accordance with the specified method and class of travel where these are specified in the Contract;

"(b) The living expenses, including any appropriate allowances, of the Contractor's employees for each day's absence from their homes, including non-working days and holidays;

"(c) The time worked, which shall be calculated by reference to the number of hours certified as worked in the time sheets signed by the Purchaser. Overtime and work on Sundays, holidays and at night will be charged at the special rates mentioned in the Contract. Save as otherwise provided, the hourly rates cover the wear and tear and depreciation of the Contractor's tools and light equipment;

"(d) Time necessarily spent on:

- (i) Preparation and formalities incidental to the outward and homeward journeys;
- (ii) The outward and homeward journeys;

(iii) Daily travel morning and evening between lodgings and the site if it exceeds half an hour and there are no suitable lodgings closer to the site;

(iv) Waiting when work is prevented by circumstances for which the Contractor is not responsible under the Contract . . ."

111. The question of the removal of the contractor's equipment and loss or damage to the equipment can be dealt with on a general basis. For example, the FIDIC-EMW Conditions deal with these two matters.

112. Clause 36.1 of FIDIC-EMW deals with the former question:

"All Contractor's Equipment provided by the Contractor shall, when brought on to the Site, be deemed to be exclusively intended for the execution of the Works and the Contractor shall not remove the same or any part thereof, except for the purpose of moving it from one part of the Site to another, without the consent in writing of the Engineer, which shall not be unreasonably withheld."

113. Clause 36.2 deals with the latter question:

"The Contractor shall be liable for loss of or damage to any of the Contractor's Equipment which may happen otherwise than through the default of the Employer."

#### IV. PASSING OF RISK

##### A. Preliminary remarks

114. The main focus of this chapter is to examine the various forms to determine the time when the risk passes to the purchaser. Usually a distinction is made between the passing of risk in the machinery and materials on the one hand, and the passing of risk in the completed works on the other.

115. The assumption of risk by the contractor means that in the event of accidental loss, damage or destruction of the works the contractor is bound to repair or replace them at his cost. The assumption of risk by the purchaser means that in the event of accidental loss or damage the purchaser must nevertheless perform his obligations under the contract. There are, however, exceptions. Risks which are unforeseen and unexpected are considered to be outside the contemplation of both parties and are, therefore, treated differently. The consequences of these risks on the parties' obligations are discussed in part two, XIII, *Exoneration*.\*

\* A/CN.9/WG.V/WP.4/Add.5 (reproduced below).

116. The forms under study do not contain any specific provision on the consequences of the passing of risk. The Sales Convention has a provision on this question, which is applicable to a works contract as well. Article 66 states:

"Loss of or damage to the goods after the risk has passed to the buyer does not discharge him from his obligation to pay the price, unless the loss or damage is due to an act or omission of the seller."

### B. *Time of the passing of risk*

#### 1. *Machinery and materials*

117. The ECE 188A/574A General Conditions deal only with the passing of risk in the machinery and materials. Under both ECE 188A/574A the time of passing of risk will depend on the types of sale.

118. ECE 574A provides for three situations:

(a) Where the contract gives no indication of the form of sale. Clause 9.1 states:

"Where no indication is given in the Contract of the form of sale, the Plant shall be deemed to be sold 'ex works'."

In this situation under clause 9.2 (a):

"... the risk shall pass from the Contractor to the Purchaser when the Plant has been placed at the disposal of the Purchaser ..."

(b) On certain specified forms of sale, clause 9.2 provides:

"(b) On a sale FOB or CIF, the risk shall pass from the Contractor to the Purchaser when the Plant has effectively passed the ship's rail at the agreed port of shipment.

"(c) On a sale 'free at frontier', the risk shall pass from the Contractor to the Purchaser when the Customs formalities have been concluded at the frontier of the country from which the Plant is exported."

(c) On other forms of sale clause 9.3 provides:

"On any other form of sale, the time when the risk passes shall be determined in accordance with the agreement of the parties."

119. ECE 188A, clause 9 makes reference to the International Rules for the Interpretation of Trade Terms (Incoterms) of the International Chamber of Commerce in force at the date of the formation of the Contract.

#### 2. *Completed works*

120. Most of the forms under study do not deal with the passing of risk in the completed works. Only clause

32.1 of FIDIC-EMW contains the following provision:

"As soon as the Works have been completed ... and have passed the Tests on Completion, the Engineer shall issue a ... 'Taking-Over Certificate' ... whereupon ... risk of loss or damage to the Works ... shall ... pass to the Employer ..."

121. Some forms do not contain provisions on passing of risk but provide for the care of the works. Clause 20 (1) of FIDIC-CEC states:

"From the commencement of the Works until the date stated in the Certificate of Completion for the whole of the Works ... the Contractor shall take full responsibility for the care thereof ..."

122. Certificates of completion may be issued in stages as each section of the works is completed. FIDIC-CEC provides that care of the contractor ceases in respect of that part for which a completion certificate is issued. Clause 20 of FIDIC-CEC provides:

"... Provided that if the Engineer shall issue a Certificate of Completion in respect of any part of the Permanent Works the Contractor shall cease to be liable for the care of that part of the Permanent Works from the date stated in the Certificate of Completion in respect of that part and the responsibility for the care of that part shall pass to the Employer ..."

123. Similar provisions are contained in clause 15.1 of FIDIC-EMW.

124. The Sales Convention contains several provisions concerning the time of the passing of risk. In general, according to article 67, "the risk passes to the buyer when the goods are handed over to the first carrier for transmission to the buyer ..."

125. For cases not within the general provisions, article 69 of the Sales Convention provides:

"... the risk passes to the buyer when he takes over the goods or, if he does not do so in due time, from the time when the goods are placed at his disposal and he commits a breach of contract by failing to take delivery."

### C. *Obligations of the contractor*

126. Until the risk passes to the purchaser the contractor is obliged to repair or replace the works at his own cost in the event of accidental loss or damage to the works.

127. Some of the forms under study expressly state this obligation of the contractor. Clause 20 of FIDIC-CEC provides:

"... In case any damage, loss or injury shall happen to the Works, or to any part thereof, from any cause whatsoever, save and except the excepted risks as



defined in sub-clause (2) of this Clause, while the Contractor shall be responsible for the care thereof the Contractor shall, at his own cost, repair and make good the same, so that at completion the Permanent Works shall be in good order and condition and in conformity in every respect with the requirements of the Contract and the Engineer's instructions . . ."

128. The wording of the relevant provisions under FIDIC-EMW is slightly different but the practical effect is the same. Clause 15.1 states:

"... in case any damage or loss shall happen to any Portion of the Works not taken over as aforesaid, from any cause whatsoever (save and except the accepted risks as defined in paragraph (b) of this Sub-Clause) the same shall be made good by and at the sole cost of the Contractor and to the satisfaction of the Engineer . . ."

129. The passing of risk will not affect the contractor's obligation for any damage caused by him after taking over. Clause 15.1 of FIDIC-EMW states:

"... The Contractor shall also be liable . . . for any loss of or damage to the Works occasioned by him or by any Sub-Contractor in the course of any operations carried out by him or by his Sub-Contractors for the purpose of completing any outstanding work or complying with his obligations . . ."

The FIDIC-CEC Conditions contain a similar provision.

## V. TRANSFER OF PROPERTY

### A. Preliminary remarks

130. This chapter describes approaches undertaken by the forms under study as regards the transfer of property in the plant or in the completed works.

131. According to the provisions of some of the forms under study property is transferred to the purchaser on one of the following occasions: when the plant is appropriated to the contract; when the plant is delivered pursuant to the contract; when the contractor becomes entitled to require that the contract price of the plant be included in an interim certificate.

### B. Various approaches to the transfer of property

132. According to the FIDIC-EMW Conditions, transfer of property in the plant will take place when one of the stipulated events first occurs. Clause 35.1 provides:

"Plant supplied or to be supplied pursuant to the Contract shall become the property of the Employer at whichever is the earlier of the following times:

"(a) When Plant is appropriated to the Contract;

"(b) When by virtue of Clause 26 (Delivery) or Clause 27 (Suspension of Works) the Contractor becomes entitled to require that the Contract Price of Plant be included in an interim certificate; or

"(c) When Plant is delivered pursuant to the Contract."

133. It may be noted that under clause 1.1(1) of FIDIC-EMW "Plant" means "machinery, apparatus, materials, articles and things of all kinds to be provided under the Contract other than Contractor's Equipment".

134. FIDIC-EMW further provides for the transfer of property in the works in connexion with the taking over. Clause 32.1 states:

"As soon as the Works have been completed . . . and have passed the Tests on Completion, the Engineer shall issue a . . . 'Taking-Over Certificate' . . . and the Employer shall be deemed to have taken over the Works . . . whereupon title to . . . the Works . . . shall . . . pass to the Employer . . ."

135. The FIDIC-CEC Conditions do not contain provisions for the transfer of property in the plant. These Conditions, however, recognize that the purchaser has an interest in ensuring the availability to the purchaser of the plant and materials needed for the works. Accordingly article 53.(1) prohibits the contractor from removing the materials once they are brought on to the construction site. It provides:

"All . . . materials provided by the Contractor shall, when brought on to the Site, be deemed to be exclusively intended for the execution of the Works and the Contractor shall not remove the same or any part thereof, except for the purpose of moving it from one part of the Site to another, without the consent, in writing, of the Engineer . . ."

136. There is a similar provision in clause 36.1 of FIDIC-EMW restricting the removal of the contractor's equipment.

137. The UNIDO model contracts do not contain provisions for the transfer of property.

138. The ECE General Conditions do not deal with the transfer of property as such, but contain a provision on retention of title in case of non-payment by the purchaser. Clause 11.3 of both ECE 188A/574A states:

"If delivery has been made before payment of the whole sum payable under Contract, Plant delivered shall, to the extent permitted by the law of the country where the Plant is situated after delivery, remain the property of the Contractor until such payment has been effected. If such law does not permit the Contractor to retain the property in the Plant, the Contractor shall be entitled to the benefit of such other rights in respect thereof as such law permits him to

retain. The Purchaser shall give the Contractor every assistance in taking any measures required to protect the Contractor's right of property or such other rights as aforesaid."

### C. Consequences of the transfer

139. Where the property in the plant is transferred to the purchaser while the contractor is still in possession of the plant the contractor has some responsibilities to protect the purchaser's property. Clause 35.2 of FIDIC-EMW provides:

"Where the property in Plant passes to the Employer prior to the delivery of such Plant the Contractor shall so far as is practicable and to the reasonable satisfaction of the Engineer set the Plant aside and mark the Plant as the property of the Employer . . . Such Plant shall be in the care and possession of the Contractor solely for the purposes of the Contract and shall not be within the ownership or disposition of the Contractor . . ."

140. Transfer of property does not imply approval of the materials by the purchaser. Under the FIDIC-EMW the purchaser retains the right under the contract to reject the materials. Clause 35.2 states:

"... any interim certificate issued by the Engineer shall be without prejudice on the exercise of any power of the Engineer contained in the Contract to reject Plant which is not in accordance with the Contract and upon any such rejection the property in the rejected Plant shall immediately revert to the Contractor."

[A/CN.9/WG.V/WP.4/Add.2\*]

## VI. TRANSFER OF TECHNOLOGY

### A. Preliminary remarks

1. The phrase "transfer of technology" is used more and more frequently in international commercial contracts whether the parties be from developed or developing countries. It encompasses a great number of things from the right to use the goods sold to the training and assistance of the purchaser's personnel so that they can operate the works. The present chapter will limit itself to the study of the situation most commonly found in contracts for the construction of large industrial works where the contractor will transfer technology, not only in

providing the plant, the equipment and the machinery but also in transferring the know-how and methods of using them.

### B. Object of the transfer of technology

#### 1. Object of the obligation

2. Of the forms studied, only the UNIDO model contracts describe substantially the object of the contract in this respect. For instance, in article 2 of UNIDO-TKL the general object of the contract includes, *inter alia*, "the grant of licence and know-how and the provision of basic and detailed engineering". UNIDO-TKL gives some indication as to what is meant by these words:

*Article 3.1.2:* "Supply of know-how and basic engineering, including but not limited to:

- "Process flow diagrams
- "Material and energy balances
- "Equipment data and specifications
- "Piping and instrument diagrams and specifications
- "Plant layout
- "Electric, steam and other distribution systems
- "Effluent and emission specifications
- "Operational manuals
- "Maintenance manuals"

*Article 3.1.3:* "The detailed engineering for the Plant."

3. Article 4.5 of UNIDO-TKL also deals with this question:

"The CONTRACTOR shall provide or obtain (as the case may be) the know-how for various processes from the Process Licensors as follows:

- Ammonia Plant (name of Licensor(s))
- Urea Plant (name of Licensor(s))
- (Specify any other, e.g. water treatment)

and shall design the Plant in conformity with the basic engineering criteria of the Process Licensors. Documentation relative to all know-how and basic engineering provided by the CONTRACTOR or obtained from the Licensors shall be provided to the PURCHASER by the CONTRACTOR."

4. Since such know-how is invariably affected by new developments there is always a possibility that such developments might occur between the time of the negotiation and signing of the contract on the one hand and the time when the documents are to be made available to the purchaser on the other. Article 4.5 of UNIDO-TKL imposes on the contractor the obligation to provide the purchaser with:

\* 21 April 1981.

"... the latest commercially proven know-how available to the Process Licensors at the time of making such documents available (such documentation to cover the state-of-the-art of the know-how at the time of the signing of the Contract, or if mutually agreed to, at a later date) and that the detailed engineering will be undertaken by the CONTRACTOR according to the latest design standards available and/or known to the CONTRACTOR at the time of design."

5. There would seem to be a slight discrepancy between article 4.5 and the last sentence of article 7.2 of the same contract which reads as follows:

"The CONTRACTOR also hereby undertakes to make available to the PURCHASER the latest know-how and techniques available to the Process Licensors at the signing of the Contract and to the CONTRACTOR at the time of design."

6. In their comments on article 4.5 of UNIDO-TKL an international group of contractors suggested that the contractor should be bound to supply only the technology he can have access to at the date of the signature of the contract.

## 2. The price

7. The price stated for the contract includes the cost of the technology the purchaser is acquiring. Neither the Sales Convention nor the ECE General Conditions nor the FIDIC Conditions make any specific reference to the price of the technology transferred. However, the UNIDO model contracts deal with this question in some detail.

8. The text of the provisions of the various UNIDO model contracts dealing with price differs depending on whether the contract is a turn-key lump-sum one, a cost reimbursable one or a semi-turn-key one. However, whatever may be the type of contract, it apportions the price and states that a certain amount of the total price relates to the granting of the licenses, know-how and supply of basic engineering. Article 20.2 of UNIDO-CRC also states which amounts apply to the Ammonia Plant, the Urea Plant, and to utilities.

9. Article 20.11 of UNIDO-CRC indicates in which manner this amount has to be paid:

"(25%) (amount) as an advance payment.

"(50%) (amount) on receipt by the PURCHASER of a copy of the know-how and basic engineering documents . . .

"(25%) (amount) on completion of the guarantee tests of the plant and issuance of the Provisional Acceptance certificate of the PURCHASER."

10. The UNIDO-CRC counter-proposal modifies greatly this apportionment. Article 20.12 provides for

the price to be payable 50%, 45%, and 5% upon the occurrence of the same events.

## 3. Further transfer of technology

11. Technological developments can intervene not only between the time of the signature of the contract and the time of the furnishing of the documents but also after the works are completed. It is in the interest of the purchaser that these developments be made available to him. Article 7.3.1 of UNIDO-TKL provides for "technological developments and improvements in operative techniques, preventive maintenance and safety measures applicable to the plant constructed pursuant to this contract and other relevant data and proprietary information to be made available to him, whether or not they become licensable by the process licensors". The purchaser will have nothing to pay for obtaining this additional information.

12. However, under article 7.3.2 of UNIDO-TKL, the purchaser will have to pay the reasonable costs involved if he wants the:

"rights to use proprietary processes developed or acquired by the CONTRACTOR including patented processes which could result in significant improvement(s) in the capacity, reliability and efficiency of the Plant, and quality of the products."

13. Depending on which UNIDO model contract is being examined, the period of time during which the obligations are imposed on the process licensors or the contractor varies: 10 years in UNIDO-TKL, 8 to 10 years in UNIDO-CRC, 5 years in the UNIDO-CRC counter-proposal. The length of this period of time should be negotiated by the parties in each specific case.

## 4. Retransfer of technology

14. Once the purchaser has taken over the plant and has started operating it, he may very well discover himself new methods or new techniques. What is his obligation towards the contractor or the process licensor in this respect? UNIDO-TKL does not impose on the purchaser any obligation towards the contractor as such; his obligation is only towards the process licensor whether he be the contractor or a third party to the contract. Under article 7.3.1:

"... The PURCHASER will also make available to the Process Licensor, free of charge, any improvements in operating techniques which the PURCHASER shall have made in the same period." (i.e. the 10 years mentioned in paragraph 13 above).

## C. Ownership of the technology to be transferred

15. The contractor may not himself be the owner of all of the technology to be transferred. He will therefore

have to obtain it from a process licensor who may not be a party to the contract; article 7.1 of UNIDO-TKL contemplates such a situation:

"The CONTRACTOR hereby affirms that it has or has obtained the unqualified right(s) to grant, and hereby does grant to the PURCHASER irrevocable, non-exclusive, non-transferable, fully paid-up licence(s) for use in the operation of all the processes . . ."

16. Article 7.2 goes on further:

"The CONTRACTOR shall ensure (through specific arrangements, with proof provided to the PURCHASER) that the Process Licensors shall make available to the PURCHASER through the CONTRACTOR all basic process data (received by the CONTRACTOR from Process Licensors) relating to the Contract, and that all basic process documentation and all drawings prepared by the CONTRACTOR shall also be made available to the PURCHASER together with copies of all documents mentioned in Article 3."<sup>1</sup>

17. And article 7.4 of UNIDO-TKL provides:

"The CONTRACTOR shall undertake to enter into specific arrangements with the Process Licensor(s) (with satisfactory proof provided to the PURCHASER) to ensure the continued availability to the PURCHASER of confidential information similar in scope and content to that provided pursuant to Article 7.3."

18. Nevertheless, however closely the process licensor may be involved in the contract he is not a party to it. Thus, there is no contractual relationship between him and the purchaser and therefore the purchaser has no contractual reason to communicate with him directly unless he is expressly authorized to do so by the contract. Such authorization is granted to the purchaser by the UNIDO-TKL in two cases:

*Article 7.2.1:* "In circumstances where the CONTRACTOR is unable or unwilling to make available to the PURCHASER the necessary process know-how and related information, the PURCHASER shall be free to approach the Process Licensor(s) directly."

*Article 7.2.2:* "The PURCHASER shall also have the right to establish direct contractual arrangements with the said Process Licensor in the event that the circumstances envisaged in Article 33 apply."<sup>2</sup>

#### D. Confidentiality

19. On account of the very nature of the technology and of the trade and industrial secrets which may be

involved and all the other information which should not be disclosed to third persons UNIDO-TKL imposes on the purchaser an obligation of confidentiality:

*Article 7.8:* "The PURCHASER agrees that he shall treat as confidential all process and technical information, proprietary know-how, patented processes, documents, data and drawings supplied by the CONTRACTOR (whether owned by the CONTRACTOR or otherwise) in accordance with this Contract, all of which is hereinafter referred to as 'confidential information'. The PURCHASER shall not without the prior approval of the CONTRACTOR divulge such confidential information available to a third party, other than required by law, and provided that when so required by law, the PURCHASER shall duly advise the CONTRACTOR."

20. The purchaser is entitled, under article 7.10 of UNIDO-TKL, to use the confidential information thus obtained for no other "purpose than for completing, operating, using, repairing, maintaining or modifying the plant(s)".

21. On the other hand, the purchaser may have given some similar information to the contractor. Article 7.10 of UNIDO-TKL imposes on the contractor a similar obligation:

". . . Similarly, the CONTRACTOR will not use or divulge any technical data or confidential information and drawings or technical documents given by the PURCHASER, his representative or Technical Advisor, to the CONTRACTOR except for the purposes strictly connected with the Contract."

22. There are exceptions to this obligation to confidentiality. One type of exemption is provided for by article 7.9.1 and 7.9.2 of UNIDO-TKL which states that the obligation does not apply to confidential information:

"Which is or becomes a part of the public domain, through no fault of the PURCHASER.

"Which is already known to the PURCHASER, his representatives or Technical Advisor, before the agreement as to confidentiality was given . . ."

23. The other type of cases where the purchaser may be released from his obligation of confidentiality occurs when he has to give access to the plant to third parties for certain specific reasons, i.e. modifications of the plant(s) which in the purchaser's opinion would result in improved or better plant operation or when the plant requires to be expanded or modernized with the incorporation of contemporary technology. In such cases, the purchaser must first ask the contractor to do the required modification, expansion or modernization. It is only in the event the contractor is unable or unwilling to do so that (under article 7.5 of UNIDO-TKL):

<sup>1</sup> Article 3 deals with the over-all scope of work and division of responsibility.

<sup>2</sup> Article 33 deals with termination or cancellation of the contract.

"... the PURCHASER shall have the right to employ or retain any other person, firm or agency to undertake and complete such work above referred to, and in such an eventuality, the PURCHASER shall not be held to be in breach of the secrecy provisions of this Article."

24. The obligation of confidentiality is limited in time by the contract. Article 7.13 of UNIDO-TKL states as follows:

"Except when otherwise agreed, the PURCHASER's obligations . . . shall be valid for a period of eight (8) years from the Effective Date of the Contract."

25. In other contracts, it is for a different period. As for the UNIDO-CRC counter-proposal, no specific period is stated. This period can also be negotiated by the parties in each specific case. The parties can also take into account other criteria as for example, the remaining time of the patent.

26. The obligation of confidentiality survives the contract in the event it is cancelled or terminated during the period provided for. (See article 7.12 of UNIDO-TKL.) This would seem to be on account of the nature of this obligation and of the type of privileged information which has been acquired by the parties under the contract.

### E. *Infringement*

27. In the same fashion the seller in a contract of sale is responsible towards the purchaser in the event a third party claims rights in the goods sold, the contractor has certain obligations in the event a third party brings a suit against the purchaser alleging a right or claim based on industrial or other intellectual property in the technology transferred.

28. The Sales Convention contemplates that the goods sold may be subject to intellectual property rights and in article 42 imposes on the seller the obligation to:

"... deliver goods which are free from any right or claim of a third party based on industrial property or other intellectual property, of which at the time of the conclusion of the contract the seller knew or could not have been unaware . . ."

29. However, this obligation exists only when the right or claim arises under the law of the State where the goods are to be resold or otherwise used and only if the parties had this in mind when they contracted, or under the law of the State where the buyer has his place of business.

30. Furthermore, under paragraph 2 of the same article:

"The obligation of the seller . . . does not extend to cases where:

"(a) At the time of the conclusion of the contract the buyer knew or could not have been unaware of the right or claim; or

"(b) The right or claim results from the seller's compliance with technical drawings, designs, formulae or other such specifications furnished by the buyer."

31. In the event a claim is made against the buyer of the goods, he can, after giving notice to the seller, avail himself of the remedies provided for under articles 44 and 45 of the Sales Convention.

32. Of the FIDIC Conditions, only the FIDIC-EMW contains provisions pertaining to this eventuality. Clause 19.1 provides as follows:

"The Contractor shall fully indemnify the Employer against all claims and proceedings for or on account of infringement of any letters patent, registered design, copyright, trade mark or trade name or industrial property right protected at the date of the Contract in the Contractor's country or in the country in which the Plant is to be erected, arising by reason of the construction of the Works or by the use of any Plant supplied by the Contractor, but such indemnity shall cover any use of the Works otherwise than for the purpose indicated by or reasonably to be inferred from the Specification or any infringement which is due to the use of any Plant in association or combination with any other plant not supplied by the Contractor."

33. The ECE General Conditions contain no such provision.

34. In UNIDO-TKL the contractor undertakes to provide guaranties as to the purchaser's being able to go on using the know-how and the process transferred under the contract. In the event a claim is made against the purchaser, article 7.17 provides:

"The CONTRACTOR shall indemnify and hold harmless the PURCHASER in connection with any liabilities arising out of patent infringement and/or matters arising out of secrecy and/or proprietary information . . ."

35. In the event a claim is made against him or a suit instituted, article 7.14 of UNIDO-TKL requires the purchaser to give prompt notice of it to the contractor, in order that the contractor can defend such a suit or claim at his own expense. The purchaser will provide all reasonable assistance but will not be responsible for any expenses except in the event he wishes to be represented by a legal counsel of his own choice.

36. The settlement of such suit or claim may be of some consequence to either the purchaser or the con-

tractor. Article 7.16 of UNIDO-TKL contemplates such a situation:

"Neither the CONTRACTOR nor the PURCHASER shall settle or compromise any suit or action without the written consent of the other if such settlement or compromise would oblige the other to make any payment or part with any property, to assume any obligation or grant any licences or other rights, or to be subjected to any injunction by reason of such settlement or compromise."

37. In order to remedy the alleged infringement, and perhaps also to avoid further litigation, the contractor has the right, under article 7.15 of UNIDO-TKL:

"... to acquire immunity from suit and to make or cause to be made alterations at its own cost to the Plant(s) to eliminate the alleged infringement provided such alteration does not prevent the Plant(s) from meeting its Performance Guarantees ..."

## VII. QUALITY

### A. Quality in works contracts

38. Quality in works contracts means the capability of the works to perform a particular function in conformity with the terms of the contract. In large industrial works the obligation to produce work of good quality is a complex issue encompassing not only the structure, dimensions, shape and location of the works but also specific details of the technical processes and products.

39. Parties to a works contract are understandably keen to ensure that their contractual obligations are as certain and as predictable as possible. The tendency in works contracts is to describe precisely the extent and quality of the work to be performed either in the main contract or in the annexed technical documents, and to use this description as a basis and measure of the contractor's work. Express provisions are likely to be made with respect to the important matters of design, the selection of materials and workmanship. Aspects of quality which parties may stipulate in the contract include the following: the dimensions, structural measurements and calculations, shape of the work, location and lay-out of the work, the choice of certain materials in relation to the intended purpose, safety requirements, performance ratings, productive capacity, quality of products, consumption of raw materials and energy. In addition to the provisions of the contract under certain forms the engineer may give additional instructions relating to the quality of the work.

40. In the forms analysed, the liabilities of the contractor in relation to design, workmanship and materials are interlinked. There can be no good workmanship if

the materials are defective. Since these aspects of quality are very specific, the precise stipulations will have to be determined by the parties' agreement. Model contracts and General Conditions cannot be expected to provide for specific details in respect of construction work. There are, nevertheless, some issues that can be dealt with in forms.

### B. Stipulation of quality

41. In most of the forms under study we find provisions stating only generally the manner of execution of the work. The clauses require that materials and workmanship are to be in conformity with the parties' agreement in so far as the agreement can be gathered from the contract. Clause 36.(1) of FIDIC-CEC provides:

"All materials and workmanship shall be of the respective kinds described in the Contract and in accordance with the Engineer's instructions ..."

42. "Contract" is defined in clause 1.(1) of FIDIC-CEC to include, *inter alia*, conditions of contract, specification, drawings and priced bills of quantity.

43. Under FIDIC-EMW, the engineer's instructions and directions are in lieu of specifications in the contract. Clause 23 provides:

"All Plant to be supplied and all work to be done under the Contract shall be manufactured and executed in the manner set out in the Specification or, where not so set out, to the satisfaction of the Engineer, and all the Works on Site shall be carried out in accordance with such reasonable directions as the Engineer may give."

44. The UNIDO model contracts deal separately with the contractor's obligations with respect to workmanship and material on the one hand, and performance of the plant on the other. Important aspects of quality relating to design, workmanship, materials and performance of the plant are guaranteed (for further details see part two, XV, *Guaranties*).\*

45. The ECE General Conditions do not contain specific provisions on the requirements relating to the quality of workmanship, design or materials. The policy of these conditions is that matters respecting the quality of the work will have to be left to the parties' agreement.

#### 1. Workmanship and material

46. Under UNIDO-CRC, the contractor has the responsibility to ensure that the plant and materials are new and in conformity with the specifications. Article 25.1 states:

"The CONTRACTOR shall be responsible for ensuring through the Purchase Orders issued to

\* A/CN.9/WG.V/WP.4/Add.6 (reproduced below).

Vendors and by inspection that the quality of the materials and workmanship of the Plant and Equipment for the Works and . . . all plant, equipment, materials, apparatus, articles, instruments, and all other goods required to be procured by the CONTRACTOR under this Contract shall be new and of the most suitable grade for the purposes intended, to the Contract and design specifications, the standards and regulations . . . and (whenever applicable) the domestic standards and regulations of the PURCHASER's country."

47. Under the ECE General Conditions the contractor also guarantees the quality of the plant during a stipulated period of time. The specific obligations of the contractor during this period are, however, not stated; it is envisaged that these will be set out in the contract. Clause 23.1 of both ECE 188A/574A states:

"Subject as hereinafter set out, the Contractor undertakes to remedy any defect resulting from faulty design, materials or workmanship."

## 2. *Performance of the plant*

48. Under the UNIDO model contracts, whether the plant has been purchased in accordance with the contractor's recommendations or supplied by the contractor, it must be capable of meeting the performance standards. Article 26.2 of UNIDO-TKL, for example, states:

"The plant supplied by the CONTRACTOR shall be capable of meeting the full requirements of normal operation, capacity, quality of Products, consumption of raw materials and utilities . . ."

49. The UNIDO model contracts contain very detailed description of requirements relating to quality. Such requirements, however, are too specific to be dealt with in General Conditions or model contracts and should be left to be determined by the parties in the contract.

50. The Sales Convention also emphasises the duty of the seller to deliver goods that are suitable for the intended or described purpose. Article 35 states:

"(1) The seller must deliver goods which are of the quantity, quality and description required by the contract . . .

"(2) Except where the parties have agreed otherwise, the goods do not conform with the contract unless they:

"(a) Are fit for the purposes for which goods of the same description would ordinarily be used;

"(b) Are fit for any particular purpose expressly or impliedly made known to the seller at the time of the conclusion of the contract, except where the circumstances show that the buyer did not rely, or that it was

unreasonable for him to rely, on the seller's skill and judgment . . ."

## C. *Execution of the project*

### 1. *Inadequacy of specifications*

51. As it has been pointed out earlier, in large industrial works, it would be in the interest of both parties to describe clearly either in the main contract or supplementary documents all the aspects of quality which the plant has to meet. Nevertheless, however detailed the description may be, it is often impossible in a works contract to foresee and make provision for all details.

52. When a dispute arises concerning the contractor's obligations, there are two questions that have to be faced: whether the contractor's obligation to complete the works free of defects should over-ride the specifications contained in the contract, and whether necessary and ancillary work omitted from the contract fall within the contractor's general obligations to complete the works.

53. The contractor is deemed to have satisfied himself as to the adequacy of his tender to perform the described work. Under the FIDIC-CEC and FIDIC-EMW Conditions the contractor is obliged to fill the gaps in the specifications so that the works will be in accordance with the contract. Clause 11 of FIDIC-CEC states:

"The Contractor shall . . . be deemed . . . to have satisfied himself, so far as is practicable, before submitting his Tender, as to the . . . extent and nature of work and materials necessary for the completion of the Works . . . and, in general shall be deemed to have obtained all necessary information . . . which may influence or affect his Tender."

### 2. *Errors in the specifications*

54. Insufficient or wrong description of the work in the specification can lead to errors in the project which may affect the quality of the work. Among the questions that arise here is whether the contractor will be obliged to modify the work, and if he does so, whether he will be entitled to extra payment.

55. The various forms analysed take different positions. In some forms the position will turn to a considerable extent on which party prepared the design or furnished the information that formed the work plan. Clause 17 of FIDIC-CEC provides:

"The Contractor shall be responsible for the true and proper setting-out of the Works in relation to original points, lines and levels of reference given by the Engineer in writing and for the correctness, subject as above mentioned, of the position, levels, dimen-



sions and alignment of all parts of the Works and for the provision of all necessary instruments, appliances and labour in connection therewith. If, at any time during the progress of the Works, any error shall appear or arise in the position, levels, dimensions or alignment of any part of the Works, the Contractor, on being required so to do by the Engineer or the Engineer's Representative, shall, at his own cost, rectify such error to the satisfaction of the Engineer or the Engineer's Representative, unless such error is based on incorrect data supplied in writing by the Engineer or Engineer's Representative, in which case the expense of rectifying the same shall be borne by the Employer . . ."

56. The relevant provision of FIDIC-EMW (clause 7.2) is similar except that it gives the contractor additional protection. The contractor is also exempt from liability if the error is based on incorrect data supplied by another contractor.

### 3. Standards

57. Parties may stipulate standards that shall be utilized in the construction, or they may have this matter to be determined by the current professional standards. In some cases standards may be determined by the mandatory national law.

58. Under both UNIDO-CRC and UNIDO-TKL, the contractor is not restricted to the standards or codes specified in the contract. He is obliged to utilize standards superior to those contained in the specifications. Article 25.4 of UNIDO-CRC provides:

"The standards and codes to be used for the Plant(s) are given in Annexure II. The CONTRACTOR shall utilize these standards (or where applicable mandatory national standards) and/or superior standards if known to CONTRACTOR . . . for the design and procurement of all plant and equipment. Wherever standards or codes are not explicitly stated in the Contract, internationally recognized standards or codes or those which have been previously used by the CONTRACTOR in a working Ammonia/Urea Plant may be used, subject to the PURCHASER being given prior notice."

59. In the event of dispute concerning the quality of standards, article 25.5 of UNIDO-CRC provides:

"In the case of a dispute arising on any matter concerning the acceptability or qualitative level of standards or Code(s) the onus shall be on the CONTRACTOR to prove to the PURCHASER the superiority or better competence of those standard(s) or code(s) recommended (or adopted) by the CONTRACTOR pursuant to this Contract."

60. As indicated above (see paragraphs 41 and 43, *supra*) under the FIDIC-CEC and FIDIC-EMW Con-

ditions the engineer may give additional instructions concerning the standards to be utilized in the work.

61. Under the ECE General Conditions requirements relating to standards are left to be determined by the parties in the contract.

### D. Finality of contract terms

#### 1. Need for variation

62. Sometimes, during erection the contractor may find that adherence to the contract specifications will not produce a plant capable of performing the intended purpose. The question is whether the contractor's obligation to comply with the plans and specifications should over-ride his obligation to construct a plant that is capable of performing the intended purposes.

63. In general the answer will depend to a considerable extent on the type of construction contract. In a turn-key contract the contractor undertakes to construct a plant with specified qualitative standards and capable of performing a particular function. The contractor will be responsible for the modification of the works at his own cost to meet performance guaranties.

64. Clause 24 of FIDIC-EMW contains express provisions for ancillary work necessitated by unforeseen technical conditions:

"If during the execution of the Works the Contractor shall encounter physical conditions, other than climatic conditions, on the Site, or artificial obstructions, which conditions or obstructions could, in his opinion, not have been reasonably foreseen by an experienced contractor, the Contractor shall forthwith give written notice thereof to the Engineer's Representative and if, in the opinion of the Engineer, such conditions or artificial obstructions could not have been reasonably foreseen by an experienced contractor, then the Engineer shall certify and the Employer shall pay the additional cost to which the Contractor shall have been put by reason of such conditions, including the proper and reasonable cost:

"(a) Of complying with any instruction which the Engineer may issue to the Contractor in connection therewith, and

"(b) Of any proper and reasonable measures approved by the Engineer which the Contractor may take in the absence of specific instructions from the Engineer

"as a result of such conditions or obstructions being encountered."

65. UNIDO-CRC makes provision for the purchaser and contractor to agree on any necessary modification

and its implication prior to the modification and re-execution of the work. Article 15.4 provides:

"The CONTRACTOR may at any time during his performance of the Contract submit to the PURCHASER for his approval written proposal(s) for a variation of the Works."

66. The UNIDO-CRC counter-proposal suggests that the clause should only stipulate a variety of circumstances in which the contractor should be entitled to claim for additional cost. According to article 15.7 the circumstances include:

"Any encounter of physical condition or artificial obstruction which has not been stipulated in the Annexures."

67. In addition the counter-proposal enumerates circumstances which can be considered to be cases of *force majeure*.

68. Under the ECE General Conditions only the consequences of changes necessitated by local administrative regulations are provided (for further details, see part two, XVIII, *Applicable law*\*).

## 2. Right to variations

69. Under FIDIC-CEC and FIDIC-EMW, the engineer has a right to issue written orders to vary the quality and quantity of the works. Clause 34.1 of FIDIC-EMW provides:

"... The Engineer shall have full power, subject to the proviso hereinafter contained, from time to time during the execution of the Contract by notice in writing to direct the Contractor to alter, amend, omit, add to or otherwise vary any of the Works. The Contractor shall carry out such variations and be bound by the same conditions, so far as applicable, as though the said variations were stated in the Specification. Provided that no such variation shall, except with the consent in writing of the Contractor and the Employer, be such as will, with any variations already directed to be made, involve a net addition to or deduction from the Contract Sum (less Provisional Sums) of more than 15 per cent thereof. In any case in which the Contractor has received any direction from the Engineer which either then or later will, in the opinion of the Contractor, involve an addition to or deduction from the Contract Sum the Contractor shall as soon as reasonably possible and where practicable, before proceeding therewith, advise the Engineer in writing to that effect. The amount to be added to or deducted from the Contract Sum shall be ascertained

and determined in accordance with the rates specified in the schedules of prices, so far as the same may be applicable, and where rates are not contained in the said schedules or are not applicable such amount shall be such sum as is reasonable in the circumstances. Due account shall be taken of any partial execution of the Works which is rendered useless by any such variation."

70. Similarly, Clause 51 of FIDIC-CEC provides:

"(1) The Engineer shall make any variation of the form, quality or quantity of the Works or any part thereof that may, in his opinion, be necessary and for that purpose, or if for any other reason it shall, in his opinion be desirable, he shall have power to order the Contractor to do and the Contractor shall do any of the following:

"(a) Increase or decrease the quantity of any work included in the Contract,

"(b) Omit any such work,

"(c) Change the character or quality or kind of any such work,

"(d) Change the levels, lines, position and dimensions of any part of the Works, and

"(e) Execute additional work of any kind necessary for the completion of the Works

"and no such variation shall in any way vitiate or invalidate the Contract, but the value, if any, of all such variations shall be taken into account in ascertaining the amount of the Contract Price."

71. A special problem arises if the variation is so extensive as to alter the scope of the original work above a certain percentage. Under the FIDIC-EMW the contractor's written consent to the variation is required if the additional work should exceed 15% of the contract price. (Clause 34.5.)

72. All UNIDO model contracts provide a procedure for determining whether a particular work falls within the contractor's obligations. Article 15 of UNIDO-CRC provides:

"15.1 Whenever the PURCHASER shall make a request to the CONTRACTOR for change in design, or where services are required to be performed by the CONTRACTOR which in the opinion of the CONTRACTOR are in addition to the services which the CONTRACTOR is obligated to perform under this Contract, or which in the CONTRACTOR's opinion require additional payment by the PURCHASER, the CONTRACTOR shall promptly advise the PURCHASER of the cost of such further services.

"15.2 If the PURCHASER agrees that the services required of the CONTRACTOR are in addition to the

\* A/CN.9/WG.V/WP.4/Add.7 (reproduced below).

CONTRACTOR's obligation under this Contract, the PURCHASER shall, (subject to negotiations as to the cost and extent of such services and effect on the time schedule, if any) agree to pay for such services in accordance with payment terms and time schedules to be mutually agreed.

"15.3 In the event that the PURCHASER and the CONTRACTOR are unable to agree on whether such required services are within the contractual obligations of the CONTRACTOR, or if the PURCHASER considers that the payment demanded for such required services by the CONTRACTOR is exorbitant, the Technical Advisor shall have the right to decide on the quantum of payment, if any, which may be payable by the PURCHASER to the CONTRACTOR. In such an eventuality the CONTRACTOR shall proceed without delay to carry out the design changes, and/or provide the services which are the subject of the dispute, pending the decision of the Technical Advisor. The decision of the Technical Advisor shall be without prejudice to the rights of the CONTRACTOR to submit the dispute to Arbitration."

73. The procedure under UNIDO-TKL and UNIDO-STC is similar.

74. The counter-proposal has a different approach. It stipulates the circumstances in which the contractor will be entitled to extra payment for the additional work. Article 15 provides *inter alia*:

"The CONTRACTOR shall be entitled to claim for additional cost and/or time delays and/or guarantees when a modification, change or variation occurs in the event of any of the following:

"15.1 Any modification, addition or deletion to the contract documents . . . unless the PURCHASER specifically demonstrates that it does not affect the CONTRACTOR's services.

"15.2 Any written request by the PURCHASER which causes a modification to any drawing, specification and document, purchase order or to the CONTRACTOR services or to the work, unless the elements already accomplished were not originally accomplished in accordance with the contract.

"15.3 Any additional engineering studies requested in writing by the PURCHASER, including those which are not followed by execution.

" . . .

"15.8 Any modification in the CONTRACTOR's services and/or the work proposed by one of the Parties accepted by the other Party, and ratified by both Parties."

## [A/CN.9/WG.V/WP.4/Add.3\*]

### VIII. INSPECTION AND TESTS

#### A. General remarks

1. The conformity of the plant with the requirements of the contract is of utmost importance for the purchaser and also in the interest of the contractor. To ensure this conformity works contracts usually contain provisions concerning inspection and examination in the course of production as well as tests before and after completion of the works.

2. The relevant part of article 38 of the Sales Convention stipulates:

"(1) The buyer must examine the goods, or cause them to be examined, within as short a period as is practicable in the circumstances.

"(2) If the contract involves carriage of the goods, examination may be deferred until after the goods have arrived at their destination."

3. In works contracts, especially one for large industrial works, the position is not as simple as that under the Sales Convention. Here it is in the interest of both parties to examine the works in the course of their production. For the contractor early examination means the possibility of curing the defects, if any, in the factory itself rather than on site. The defects would be easier to remedy and less expenses would be incurred. For the purchaser early rectification of defects means avoidance of subsequent delays and difficulties.

4. Works contracts, therefore, often contain provisions concerning the extent of inspection during production of machines and equipment, place and time of inspection, procedure for inspection, obligations and rights of purchaser, duties of contractor, costs of inspection, certification, and legal effect of inspection.

5. Regarding performance tests works contracts usually contain provisions concerning pre-conditions for performance tests, date of performance tests, procedure to be followed, participants, obligations of purchaser in preparation of tests, effects of tests, procedure in case of non-performed or non-successful tests, and protocol.

#### B. Inspection during production

##### 1. Rights and obligations

6. The general conditions and model forms under study adopt different approaches to the question of

\* 17 March 1981.

"inspection", "checking", "examination" and "test". The ECE General Conditions provide for inspection by the purchaser or his representative but an express agreement by the parties is required in the contract. Furthermore, the ECE General Conditions grant to the contractor a right of inspection, whereas the FIDIC Conditions give the right of inspection to the purchaser. The UNIDO model contracts on the other hand speak of the duty of the contractor to inspect and grant to the purchaser the right of participation.

7. Clause 8.1 of both ECE 188A/574A states:

*"If expressly agreed in the Contract, the Purchaser shall be entitled to have the quality of the materials used and the parts of the Plant, . . . inspected and checked by his authorized representatives . . ."*

Here the inspection is related to the quality of the materials used and the parts of the plant. Whether the words "inspection" and "checking" denote different activities is not clear.

8. Other provisions of ECE 188A/574A relate to tests. These tests are obviously carried out by the contractor, in contrast to the aforementioned inspection which is carried out by the purchaser or on his behalf. The tests according to clause 8.3 also require an express agreement by the parties.

9. Another provision of ECE 188A/574A relates to inspection on the site. Article 18.1 provides:

*"Until the Works are taken over and during any work resulting from the operation of the guarantee the Contractor shall have the right at any time during the hours of work on the site to inspect the Works at his own expense. In proceeding to the site, the inspectors shall observe the regulations as to movement in force at the Purchaser's premises."*

10. Clause 36(1) of FIDIC-CEC states:

*"All materials and workmanship . . . shall be subjected from time to time to such tests as the Engineer may direct . . ."*

And clause 25.1 of FIDIC-EMW contains the provision:

*"Unless otherwise agreed in the Contract the Engineer shall be entitled during manufacture to inspect, examine and test . . . the materials and workmanship and check the progress of manufacture of all Plant to be supplied under the Contract . . ."*

11. Whereas the ECE General Conditions speak only of the materials the FIDIC Conditions include the workmanship and even the progress of manufacture of the plant.

12. In the UNIDO models it is the contractor who is responsible for the inspection. Article 14 of UNIDO-TKL shall serve as an example; UNIDO-STC is almost

identical, whereas UNIDO-CRC is substantially shorter. Article 14.1 of UNIDO-TKL reads:

*"The CONTRACTOR shall assume full responsibility for the inspection, testing and certification of all equipment, materials, spare parts and other items . . . for incorporation into the Works. . . . [T]he CONTRACTOR shall be liable for the proper, adequate and sufficient conduct of the functions envisaged in this Article . . ."*

13. Apart from the responsibility of the contractor for the inspection of his own equipment, he has to examine the materials supplied by the purchaser. According to article 14.9 of UNIDO-TKL:

*"The CONTRACTOR shall . . . review the quality of the items being supplied by the PURCHASER as listed in Annexure VIII and elsewhere in the present Contract, . . . and shall fully satisfy himself as to whether the specifications of the technical documents supplied by the CONTRACTOR have been met . . ."*

14. The purchaser's right of inspection may extend to buildings. For example article 14.11 of UNIDO-TKL states:

*"The PURCHASER shall have the right to inspect all buildings and Civil Works during and after construction, (except for minor items such as painting etc. which may be inspected subsequently) . . ."*

15. And article 14.12 of UNIDO-TKL adds:

*"The PURCHASER shall have the right to inspect all the erection of plant and machinery, and all piping, instrumentation, electrical installation and wiring, insulation, painting and all other work connected with erection as detailed in Annexure XXIX."*

2. *Place and time of inspection*

16. Place and time are interrelated. If the place of inspection is in the factory, it must be conducted before shipment. Of course the time of inspection must be fixed according to the place where the equipment is situated for inspection. All the general conditions and contract forms under study contain provisions in regard to the place and time of inspection.

17. According to clause 8.1 of both ECE 188A/574A, the inspection and checking during manufacture and on completion,

*"shall be carried out at the place of manufacture during normal working hours after agreement with the Contractor as to date and time."*

18. As regards tests, the same General Conditions state:

*Clause 8.3: "Tests provided for in the Contract other than taking-over tests will be carried out, unless otherwise agreed, at the Contractor's works and during normal working hours."*

19. Clause 25.1 of FIDIC-EMW provides that inspection during manufacture must take place "on the Contractor's premises during working hours". The clause further provides:

"and if part of the said Plant is being manufactured on other premises the Contractor shall obtain for the Engineer permission to inspect, examine and test as if the said Plant were being manufactured on the Contractor's premises."

20. Clause 36(1) of FIDIC-CEC provides for tests "at the place of manufacture or fabrication, or on the Site or at such other place or places as may be specified in the Contract, or at all or any of such places."

21. Usually, the time of inspection will be agreed between the parties. Clause 25.2 of FIDIC-EMW provides:

"The Contractor shall agree with the Engineer the date on and the place at which any Plant will be ready for testing as provided in the Contract . . . The Engineer shall give the Contractor 24 hours' notice in writing of his intention to attend the tests."

22. ECE General Conditions provide:

*Clause 8.4:* "The Contractor shall give to the Purchaser sufficient notice of the tests to permit the Purchaser's representatives to attend."

23. Clause 38(1) of FIDIC-CEC provides for the situation involving covering up of works:

"No work shall be covered up or put out of view without the approval of the Engineer or the Engineer's Representative and the Contractor shall afford full opportunity for the Engineer or the Engineer's Representative to examine and measure any work which is about to be covered up or put out of view and to examine foundations before permanent work is placed thereon. The Contractor shall give due notice to the Engineer's Representative whenever any such work or foundations is or are ready or about to be ready for examination and the Engineer's Representative shall, without unreasonable delay, unless he considers it unnecessary and advises the Contractor accordingly, attend for the purpose of examining and measuring such work or of examining such foundations."

24. The FIDIC-CEC Conditions contain a provision on the time and place of inspection which might not find general approval in the context of the construction of big plants:

*Clause 37:* "The Engineer and any person authorized by him shall at all times have access to the Works and to all workshops and places where work is being prepared or from where materials, manufactured articles or machinery are being obtained for the Works and the Contractor shall afford every facility for and every assistance in or in obtaining the right to such access."

25. Such an unlimited right of access would certainly be opposed in some industries. In the course of preparation of the ECE General Conditions 188 an *unlimited* right was given to the purchaser for inspection at the contractor's premises. This was opposed for reasons of commercial secrecy and considerations of national defence.<sup>1</sup>

26. Article 14.1 of UNIDO-TKL deals with inspection and testing "during manufacture and prior to despatch, prior to and during inspection and upon arrival at the plant site".

27. According to article 14.3.1 of UNIDO-TKL the contractor "shall issue such confirmation to the PURCHASER's inspectors prior to their inspection, when the equipment, machinery or material is ready for final inspection."

Article 14.5 provides:

"When any equipment is ready for inspection, the CONTRACTOR shall give at least forty-five (45) days notice to the PURCHASER's representative of the time, place and goods to be inspected. Should the PURCHASER's representative desire to be present the CONTRACTOR shall be advised within thirty (30) days thereafter."

28. In their comments the group of contractors felt it a waste of time that notice be given for "any" equipment and suggested the restriction of the notice to "equipment designated to be inspected".

29. UNIDO-TKL further distinguishes inspections and tests in regard to their various places and times:

*Article 14.5.1: "Inspection and Tests at Factory.* All work shall be subject to inspection and testing at CONTRACTOR's factory and shall conform to the requirements of the Contract."

*Article 14.5.2: "Inspection and Tests at Site.* All work shall be subject to inspection and testing on Site and shall conform to the requirements of the Contract. After installation of the Work on Site, the CONTRACTOR shall carry out such required tests to prove compliance with the Contract, notwithstanding any tests which may have been carried out earlier at CONTRACTOR's factory."

*Article 14.5.3: "Inspection and Tests on Mechanical Completion.* Pursuant to the provisions of Article 18, the CONTRACTOR shall, upon due notice to the PURCHASER of his readiness to undertake the tests to demonstrate and prove completion of the Works, proceed forthwith to commence the procedures in accordance with the requirements of Article 18, but subject to the provisions referred to therein."

<sup>1</sup> See E/ECE/169, Commentary on the General Conditions for the Supply of Plant and Machinery for Export, para. 7.

30. The UNIDO models also contain the right of unlimited access to the premises of the contractor and any sub-contractors. For example in article 14.6 of UNIDO-TKL:

"All equipment, machinery, material and work performed in connexion with this Contract shall be available for inspection by the PURCHASER (through his duly authorized representative, including his underwriters as the case may be). The CONTRACTOR, its sub-contractors, and/or suppliers shall provide safe and necessary access for the inspection envisaged by this Article. The PURCHASER shall be afforded full and free access to the shops, factories, site or places of business of the CONTRACTOR, the sub-contractors and/or suppliers for such inspection to determine the condition and progress of work under the Contract."

31. The above-mentioned inspection of the items supplied by the purchaser according to article 14.9 of UNIDO-TKL must be carried out "after notice from the purchaser . . . as soon as they shall have been manufactured (but prior to beginning of the erection of each item) . . ."

### 3. Procedure for inspection

32. It may prove essential to agree on the procedure to be employed for inspections and tests and perhaps even the instruments to be used. However, "[i]f the technical requirements of the test are not specified in the Contract", clause 8.3 of both ECE 188A/574A provides, "the tests will be carried out in accordance with the general practice obtaining in the appropriate branch of the industry in the country where the Plant is manufactured".

33. The FIDIC Conditions contain no provision on procedure, but in the FIDIC Notes it is stated: "It is, of course, most important that details of inspection and testing requirements should be laid down in the specification in order that there is an agreed procedure . . ."<sup>2</sup>

34. The UNIDO model contracts leave the procedure for the contractor to decide. Article 14.5 of UNIDO-TKL merely provides:

"Wherever required by the PURCHASER, the CONTRACTOR shall associate the PURCHASER or his representative with such inspection, and shall undertake the necessary co-ordination for joint inspections."

But the purchaser may choose additional methods. Article 14.13 of UNIDO-TKL reads:

"During all inspection, the PURCHASER or his representatives may have recourse to such tests as they

may consider necessary in order to establish whether the materials, objects, supplies or methods of construction and erection are of the requisite quantity and quality . . ."

### 4. Objections and rights of purchaser

35. If in the course of inspection of the equipment it turns out that certain parts are defective, it would be in the interest of the contractor to replace them. But there might be differences of opinion between the contractor and the purchaser on the extent of defects or indeed, whether there are in fact any defects.

36. Some forms request the purchaser to give his objections with reasons in writing. Clause 8.2 of both ECE 188A/574A provides:

"If as a result of such inspection and checking the Purchaser shall be of the opinion that any materials or parts are defective or not in accordance with the Contract, he shall state in writing his objections and the reason therefor."

Similarly article 25.5 of FIDIC-EMW provides:

"If as a result of such inspection, examination or test of the Plant (other than a Test on Completion under Clause 29) the Engineer shall decide that such Plant is defective or not in accordance with the Contract he shall notify the Contractor accordingly stating in writing his objection and reasons therefor."

37. In the UNIDO-TKL it appears that the purchaser can reject the work by giving notice in writing but without a statement of reasons therefor. Article 14.6 of UNIDO-TKL reads:

"If any services or workmanship supplied by the CONTRACTOR, the sub-contractors and/or suppliers are determined by the PURCHASER, either during the performance of the work, on inspection, or during any applicable warranty period(s), to be defective and not complying with requirements of this Contract and arising out of the fault or negligence of the CONTRACTOR, the sub-contractors and/or suppliers, the PURCHASER shall notify the CONTRACTOR in writing that such work is being rejected."

38. This article is criticized by the "international group of contractors" as the purchaser is made the sole judge as to whether any service or workmanship is defective and he is also given the unilateral right of rejection without giving reasons. Moreover, it is doubtful whether the purchaser may "reject" any part during the warranty period, i.e. after taking-over and acceptance.

39. Article 14.13 of UNIDO-TKL further states:

"The PURCHASER or his representatives may require the replacement or repair, as the case may be, of items which do not conform with the Contract, even after they have been incorporated into the Works, and

<sup>2</sup> Notes on Documents for Electrical and Mechanical Works Contracts, 1980, p. 28.

the provisions of the Contract referred to in Article 14.8 shall apply *mutatis mutandis*."

According to this provision the purchaser may request replacement or repair although the contractor is not obliged to meet the purchaser's requirements. Article 14.8 of UNIDO-TKL states:

"In case of a difference of opinion, the CONTRACTOR may proceed to act on his own responsibility as regards the despatch of such goods and equipment, but subject however, to the relevant provisions of Article 25 and Articles 27 to 30 inclusive."

### 5. Duties of the contractor

40. The contractor usually will replace items which have been found defective during inspections. The general conditions and model forms contain not only obligations to that effect but also deal with the time required. Clause 8.5 of both ECE 188A/574A provides:

"If on any test (other than a taking-over test as provided for in Clause 21) the Plant shall be found to be defective or not in accordance with the Contract, the Contractor shall with all speed and at his own expense (including any transport expenses) make good the defect or ensure that the Plant complies with the Contract. Thereafter, if the Purchaser so requires, the test shall be repeated."

Similarly, clause 25.2 of FIDIC-EMW states:

"The Contractor shall with all speed make good the defect or ensure that the Plant complies with the Contract. Thereafter, if required by the Engineer, the tests shall be repeated under the same terms and conditions."

41. If under article 14.6 of UNIDO-TKL the purchaser has rejected "any services or workmanship . . . the CONTRACTOR shall, at his own expense, promptly remove and replace or correct such defective work by making the same comply strictly with all requirements."

And article 14.8 of UNIDO-TKL states:

"Should the PURCHASER's representative establish during inspection any deficiency in the inspected items, the CONTRACTOR shall take immediate steps to eliminate them. The CONTRACTOR shall maintain records of deficiencies noted and corrected."

### 6. Costs of inspection

42. The inspection will involve various kinds of expenses: costs of the contractor and of the purchaser; costs of materials; personal costs; costs at the contractor's premises or at site; costs for the first inspection, costs for a re-inspection after the removal of

the defects. Not all these are dealt with in the various general conditions and forms.

43. According to clause 8.6 of both ECE 188A/574A the contractor shall

"Unless otherwise agreed . . . bear all the expenses of tests carried out in his works, except the personal expenses of the Purchaser's representatives."

44. Clause 25.3 of FIDIC-EMW deals not only with the financial but also the technical side of the matter:

"Where the Contract provides for tests on the premises of the Contractor or of any Sub-Contractor the Contractor shall provide such assistance, labour, materials, electricity, fuel, stores, apparatus and instruments as may be requisite and as may be reasonably demanded to carry out such tests efficiently."

45. The FIDIC Conditions seem to place personal expenses on each party like the ECE General Conditions. However, if a test has to be repeated after the removal of defects "all reasonable expenses to which the Employer may be put by the repetition of the tests shall be deducted from the Contract Sum." (Clause 25.5 of FIDIC-EMW).

46. The other FIDIC Conditions deal extensively with this matter. Article 36 of FIDIC-CEC provides:

"(1) . . . The Contractor shall provide such assistance, instruments, machines, labour and materials as are normally required for examining, measuring and testing any work and the quality, weight or quantity of any material used and shall supply samples of materials before incorporation in the Works for testing as may be selected and required by the Engineer.

"(2) All samples shall be supplied by the Contractor at his own cost if the supply thereof is clearly intended by or provided for in the Contract, but if not, then at the cost of the Employer.

"(3) The cost of making any test shall be borne by the Contractor if such test is clearly intended by or provided for in the Contract and, in the cases only of a test under load or of a test to ascertain whether the design of any finished or partially finished work is appropriate for the purposes which it was intended to fulfil, is particularised in the Contract in sufficient detail to enable the Contractor to price or allow for the same in his Tender.

"(4) If any test is ordered by the Engineer which is either

"(a) Not so intended by or provided for, or

"(b) (In the cases above-mentioned) is not so particularised, or

"(c) Though so intended or provided for is ordered by the Engineer to be carried out by an independent person at any place other than the Site or the place of manufacture or fabrication of the materials tested,

<sup>3</sup> Those articles concern guarantees, warranties, liquidated damages etc.



"then the cost of such test shall be borne by the Contractor, if the test shows the workmanship or materials not to be in accordance with the provisions of the Contract or the Engineer's instructions, but otherwise by the Employer."

47. A special situation could arise in connexion with the covering up of civil engineering work. If this has to be uncovered at the request of the purchaser the costs will be borne by the purchaser if no defect is found and by the contractor if a fault is detected.

Clause 38.2 of FIDIC-CEC provides:

"The Contractor shall uncover any part or parts of the Works or make openings in or through the same as the Engineer may from time to time direct and shall reinstate and make good such part or parts to the satisfaction of the Engineer. If any such part or parts have been covered up or put out of view after compliance with the requirement of sub-clause (1) of this Clause and are found to be executed in accordance with the Contract, the expenses of uncovering, making openings in or through, reinstating and making good the same shall be borne by the Employer, but in any other case all costs shall be borne by the Contractor."

48. UNIDO-TKL contains very special requirements:

*Article 14.14:* "The CONTRACTOR shall place at the disposal of the PURCHASER, free of charge, such instruments, and in particular equipment for the radioactive check of welds, along with specialized operating staff, if requested by the PURCHASER, to enable the PURCHASER to carry out his inspection of the CONTRACTOR's work or supplies, efficiently."

The comment of the "international group of contractors" relates to the costs of such equipment which in their view should be borne by the purchaser if such instruments are not already in the possession of the contractor.

## 7. Certification

49. Both ECE 188A and 574A speak of a test report which has to be prepared by the contractor and which, in practice, would usually be signed by both parties, but which "shall be accepted as accurate by the Purchaser" in case he fails to be represented at the tests (clause 8.4).

50. Under clause 25.4 of FIDIC-EMW it is not the contractor, but the purchaser who issues the certificate:

"As and when Plant shall have passed the tests referred to in this Clause the Engineer shall furnish to the Contractor a certificate in writing to that effect."

51. In the UNIDO-TKL the contractor who is responsible for the inspection would also be responsible for the certification. According to article 14.3.2 the contractor,

"shall issue proper *Certificates of Inspection* in respect of all items of Plant and Equipment respectively, before despatch, and shall send copies of such Certificates to the PURCHASER, and *certificates of tests* carried out in connection with the issue of such Certificates of Inspection."

It is not clear whether there is a difference between certificates of inspection and certificates of tests, and what tests are necessary in *connexion with the issue* of certificates.

52. The ECE General Conditions are silent on the need to obtain certification from suppliers but provision is made in the UNIDO model forms. Article 14.2.3 of UNIDO-TKL provides that the contractor

"shall require its suppliers to provide the necessary test certificates in proper form together with all other documents required by the Inspecting Authorities in the country of manufacture or as may be required by the PURCHASER in consideration of the regulations in force in (country) and/or as provided for in the specifications."

## 8. Legal effect of inspection

53. As mentioned earlier, the requirement of inspection is in the interest of both parties. The contractor's liability for breach of obligations usually remains despite inspection by the purchaser. Indeed, some model forms provide that failure by the purchaser to inspect does not prejudice his rights against the contractor under the contract.

54. Clause 25.1 of FIDIC-EMW provides:

"Such inspection, examination or testing if made shall not release the Contractor from any obligation under the Contract."

55. Article 14.5 of UNIDO-TKL puts it thus:

"The presence of the PURCHASER's representatives shall not in any manner qualify the CONTRACTOR's obligation under this Contract. The presence of the PURCHASER's representatives also shall not in any way imply contractual acceptance of goods or transfer of ownership."

And again in article 14.17 of UNIDO-TKL:

"The inspection by the PURCHASER and/or repair or replacement of equipment or construction works at the request of the PURCHASER shall not excuse the CONTRACTOR from the liabilities, warranties or guarantees as expressed in this Contract."

56. Different provisions are contained in the various forms in relation to the non-participation of the

purchaser. According to article 8.4 of both ECE 188A/574A:

"If the Purchaser is not represented at the tests, the test report shall be communicated by the Contractor to the Purchaser and shall be accepted as accurate by the Purchaser."

57. The FIDIC-BMW Conditions provide in clause 25.2:

"... and unless the Engineer shall attend at the place so named on the date agreed the Contractor may proceed with the tests, which shall be deemed to have been made in the Engineer's presence, and shall forthwith forward to the Engineer duly certified copies of the test readings."

58. The UNIDO models follow a different approach. Article 14.6 of UNIDO-TKL provides:

"Neither the failure to make such inspection nor failure to discover defective workmanship, materials or equipment, nor approval of, or payment to the CONTRACTOR for such work, materials or equipment (pursuant to this Contract) shall prejudice the rights of the PURCHASER thereafter to require correction, replacement or reject the same as herein provided."

And again in article 14.7:

"If the PURCHASER waives his right of inspecting or testing as herein provided, it shall in no way relieve the CONTRACTOR of full liability for the quality, proper operation and performance of the completed work, and/or sections or parts thereof, nor shall it prejudice or affect the rights of the PURCHASER set forth under the Contract."

### C. *Taking-over or performance tests*

#### 1. *General remarks*

59. After completion of the works, taking-over or performance tests are usually carried out. The nature and duration of the tests depend to a large extent on the kind of performance expected of the plant.

60. ECE 188A/574A provide for taking-over tests. These tests are required to be carried out "unless otherwise agreed" (clause 21.1 respectively). On the other hand, during manufacture a special agreement in the contract is necessary.

61. FIDIC-EMW provides for tests on completion (clauses 29.1 to 29.6) whereas FIDIC-CEC leaves the question to the parties (clause 48.1).

62. Besides the above-mentioned inspections and tests the UNIDO models distinguish between mechanical completion tests (article 18) and performance guarantee

tests (article 26). According to article 18.7 of UNIDO-TKL:

"the pre-commissioning of the Plants ... and the carrying out of the Mechanical Completion Tests shall consist of the carrying out of such operations and making of such tests as are detailed in Annexure XX to establish the correct mechanical functioning of the Plants."

And article 26.2 of UNIDO-TKL provides:

"The plant supplied by the CONTRACTOR shall be capable of meeting the full requirements of normal operation, capacity, quality of Products, consumption of raw materials and utilities, all of which ... shall be proven and demonstrated by test runs as specified in this Article and in the Annexures and Specifications (provided that the Plant is operated in accordance with the contractor's technical directions and instructions), and that such test runs are conducted in accordance with the conditions set forth herein."

#### 2. *Time for performance tests*

63. Usually it is the contractor who decides on the time for performance tests (in the absence of stipulations in the contract). According to clause 21.1 of both ECE 188A/574A,

"the Contractor shall notify the Purchaser in writing when the Works will be ready, and such notification shall be in sufficient time to enable the Purchaser to make any necessary arrangements."

64. Clause 29.1 of FIDIC-EMW is more specific as to what constitutes sufficient time:

"The Contractor shall give to the Engineer, with a copy to the Employer, 21 days' notice in writing of the date after which he will be ready to make the Tests on Completion. Unless otherwise agreed the tests shall take place within 10 days after the said date on such day or days as the Engineer shall notify the Contractor in writing."

65. UNIDO-TKL does not mention any period in regard to mechanical completion tests, but requires 45 days' notice for performance tests:

*Article 18.3:* "As soon as any parts of the Works or Plant or any part thereof, is in the opinion of the CONTRACTOR substantially complete and ready for inspection the CONTRACTOR shall notify the PURCHASER (by means of a Construction Completion Report) that the Plant or a section thereof is ready for Mechanical Completion Tests." And,

*Article 14.10:* "Where the CONTRACTOR or any of his sub-contractors are undertaking any performance tests of any equipment to be supplied under this Contract, or any tests required under statutory law, the CONTRACTOR shall give at least forty-five (45)

days notice of such tests to the PURCHASER, or his representatives if such have been designated, and if desired the said representatives shall be present at such tests."

Furthermore the commencement of the performance test is connected with the start-up of the plant. Article 26.10.1 provides:

"The first twenty (20) day test of Ammonia and/or Urea Plant shall commence within ninety (90) days from the Start-up of the Plant(s), . . ."

### 3. Procedure for performance tests

66. The procedure to be followed for performance tests depends on the performance guarantee, if any, and is therefore usually agreed upon between the parties. Clause 21.2 of both ECE 188A/574A refers, in the absence of contractual provisions, to general practice:

"The tests shall take place in the presence of both parties. The technical requirements shall be as specified in the Contract or, if not so specified, in accordance with the general practice existing in the appropriate branch of the industry in the country where the Plant is manufactured."

67. Clause 29.2 of FIDIC-EMW implies that the tests shall be carried out in the presence of both parties (i.e. contractor and engineer acting on behalf of the purchaser) but is silent in regard to the technical requirements.

68. As mentioned already, the UNIDO model forms distinguish between mechanical completion tests and performance tests. According to article 18.3 of UNIDO-TKL the construction completion report

"shall indicate which parts of the Works or the Plant the CONTRACTOR proposes to demonstrate, have been completed in accordance with the specifications and have passed initial inspection tests as may have been specified in the Contract. The CONTRACTOR shall prepare and submit a programme of tests to prove the individual equipment and/or section, of a Plant."

69. The procedure for the tests has to be agreed between the parties and article 18.6 of UNIDO-TKL contemplates a subsequent review:

"When all the items of equipment in a Plant or any of the sections of the Off-sites and Utilities are ready and have been completed pursuant to this Contract (viz. erected, installed and tested), the CONTRACTOR and PURCHASER shall review the procedures for the pre-agreed tests for the demonstration of the Mechanical Completion of the Plant to be undertaken in accordance with Annexure XX (or otherwise) and the detailed procedures therewith."

70. Article 18.8 of UNIDO-TKL also makes provision for the question of who is responsible for the tests:

"The operations and tests referred to in 18.6 and 18.7 above shall be carried out in a competent manner by the CONTRACTOR's personnel under its direction and responsibility and in the presence of the PURCHASER's personnel."

71. In regard to performance tests UNIDO-TKL is more specific. Article 26.9 provides:

"The procedures to be followed for the execution of the Guarantee Tests shall be agreed upon between the parties three (3) months before the commencement of the above tests. Instruments tolerances shall be warranted by the CONTRACTOR. The PURCHASER shall have the right to specify instruments with low margin of tolerance for measurement of the Plant capacity and consumptions."

72. UNIDO-TKL does not specify whose personnel is to carry out the performance tests but article 26.10 provides that "the Performance Guarantee Tests of the Plants shall be run under the direction and supervision of the CONTRACTOR's personnel." Also,

"all measurements will be taken jointly by the PURCHASER and the CONTRACTOR and in the event of any dispute relating only to the correctness, sufficiency and/or adequacy of the tests and/or in the manner in which the tests were conducted, the provisions of article 37 shall apply."<sup>4</sup>

73. Since the performance test is to be carried out over a certain period UNIDO-TKL provides for adjustments to be made to the plant during that period:

*Article 26.10.3:* "The CONTRACTOR shall have the right to have the Plant(s) operated in accordance with its requirements at its own risk during the period to the CONTRACTOR to perform the test(s) and the PURCHASER's personnel shall work under the directions and technical instructions of the CONTRACTOR."

The purchaser on the other hand "shall have the right to operate the Plants as and when such operation shall not interfere with the CONTRACTOR's work."

74. UNIDO-TKL stipulates the aim of the performance test—the demonstration of a sustained steady operation of the plant over a specified continuous period (article 26.3.3). The capacity of the plant, its capability of producing specified products as well as the consumption of raw materials and utilities must be demonstrated (article 26.8).

### 4. Obligations of purchaser concerning performance tests

75. It is usually the responsibility of the purchaser to provide the personnel, materials, power etc., for the

<sup>4</sup> Article 37 deals with settlement of disputes and arbitration.

purpose of carrying out the performance test. Clause 21.3 of both BCE 188A/574A provides:

"Subject to the provisions of paragraph 2 hereof the Purchaser shall free of charge provide any power, lubricants, water, fuel and materials of all kinds reasonably required for final adjustments and for taking over tests. He shall also install free of charge any apparatus necessary for the above-mentioned operations."

76. Similarly, clause 29.4 of the FIDIC-EMW provides:

"The Employer, except where otherwise specified, shall provide free of charge subject to the provisions of Sub-Clause 5 of this Clause such labour, materials, electricity, fuel, water, stores and apparatus as may be requisite and as may be reasonably demanded to carry out such tests efficiently."

77. The UNIDO-TKL model contract regulates the obligation of the purchaser in great detail:

*Article 5.7:* "The PURCHASER shall provide free of charge all the raw materials, fuel, consumable items and make-up items necessary for the testing, commissioning, operation and maintenance of the Plant unless otherwise specifically mentioned in the specification or elsewhere in the Contract as to be supplied by the CONTRACTOR."

*Article 5.8:* "The PURCHASER shall provide all feedstocks, outside utilities, chemicals and other materials required for the operation of the Plant except the first charge of catalysts and chemicals to be supplied by the CONTRACTOR within his scope of supply. The feedstocks shall be in accordance with the specifications contained in this Contract or as otherwise agreed. The maximum quantity per hour and conditions of outside utilities (power, water, etc.) will be intimated by the CONTRACTOR to the PURCHASER within six (6) months of the Effective Date of the Contract. The requirement of all chemicals and other material inputs required for the start-up of the Plant and regularly thereafter, shall be intimated by the CONTRACTOR to the PURCHASER at least nine (9) months before the Mechanical Completion of the Plant."

*Article 5.9:* "The PURCHASER shall provide free of charge operation and maintenance personnel for the CONTRACTOR throughout the period from the beginning of the mechanical testing of equipment till the date of Acceptance of the Plant in numbers and of competence corresponding to the manning requirements which are to be developed by the CONTRACTOR in the form of a Manpower and Qualification Chart and approved by the PURCHASER."

##### 5. Unperformed performance test

78. If no performance test is carried out within the period stipulated in the contract this can be due to

reasons for which either one or none of the parties would be responsible.

79. If the contractor does not carry out the agreed tests the FIDIC-EMW Conditions provide that the engineer on behalf of the purchaser may proceed to make the tests:

"If in the opinion of the Engineer the tests are being unduly delayed he may, by notice in writing, call upon the Contractor to make such tests within 21 days from the receipt of the said notice, and the Contractor shall make the said tests on such days within the said 21 days as the Contractor may fix and of which he shall give notice to the Engineer. If the Contractor fails to make such tests within the time aforesaid the Engineer may himself proceed to make the tests. All tests so made by the Engineer shall be at the risk and expense of the Contractor unless the Contractor shall establish that the tests were not being unduly delayed in which case tests so made shall be at the risk and expense of the Employer." (Clause 29.3.)

80. UNIDO-TKL contains several provisions concerning tests not performed by the contractor, for instance,

*Article 18.17:* "If for reason attributable to the CONTRACTOR (whether directly or indirectly), the CONTRACTOR is unable to demonstrate any or all of the Guarantee Tests and/or Performance Requirements referred to in Article . . . the provisions of Articles 27.2 to 27.5 (inclusive) (as the case may be) shall apply . . ." This means the contractor has to pay liquidated damages. Or:

*Article 26.10.2:* "If, for reasons ascribable to mistake(s) and/or error(s) in process and/or detailed engineering or for any other reasons related to the work and services provided or performed by the CONTRACTOR, and/or mistake(s) and error(s) in the Contractual Specifications and instructions, the CONTRACTOR is not able to perform the test(s) within the period(s) stated in Article 26.10.1 above, the provisions of Article 26.11 shall apply."

81. In any event, according to article 18.1 of UNIDO-TKL,

"If Guarantees and/or Performance Guarantee Tests and/or any of the tests or pre-commissioning tests required are not capable of being commenced, undertaken, met or completed for reasons attributable to the CONTRACTOR's work and/or services, . . ." then

"The CONTRACTOR shall be responsible . . . for undertaking repairs and modification(s) of the Plant(s) and/or of any of the sections and/or parts thereof, in relation to any part of the Work(s) supplied by him or for which he is responsible under this Contract . . ."

82. UNIDO-TKL also foresees the possibility that the tests have to be made subsequently for reasons not attributable to the contractor. Under these circumstances the contractor is still obliged to demonstrate the tests, but article 26.16 of UNIDO-TKL makes provision for the costs:

"In the event the Performance and Guarantee Tests cannot be made within the period stipulated in Article 26.14 above, the CONTRACTOR shall be obligated to send personnel to Site to start up the Plant and to undertake tests on the Plant provided however that the PURCHASER shall pay additional fees and travel expenses for this service as may be agreed between PURCHASER and CONTRACTOR."

83. Where the tests cannot be performed due to reasons solely attributable to the purchaser the contractor is not obliged to undertake all future tests. Article 26.14 of UNIDO-TKL provides:

"The obligations of the CONTRACTOR (subject to Articles 18, 28, 29 and 32) shall be deemed to have been fulfilled if for reasons attributable solely to the PURCHASER, the first Guarantee Test cannot be carried out within eighteen (18) months from the Mechanical Completion of the Plant."

#### 6. Unsuccessful performance test

84. If a performance test proves unsuccessful for reasons attributable to the work of the contractor then he has to remedy the defects and he is usually entitled to another test. The parties have to agree on the number of tests and on the question of costs.

85. Clause 21.2 of both ECE 188A/574A provides:

"If as a result of such tests the Works are found to be defective or not in accordance with the Contract, the Contractor shall with all speed and at his own expense make good the defect or ensure that the Works comply with the Contract, and thereafter, if the Purchaser so requires, the test shall be repeated at the expense of the Contractor."

Similarly, clause 29.5 of FIDIC-EMW reads:

"If any Portion of the Works fails to pass the tests, tests of the said Portion shall, if required by the Engineer or by the Contractor, be repeated within a reasonable time upon the same terms and conditions, save that all reasonable expenses to which the Employer may be put by the repetition of the tests shall be deducted from the Contract Sum."

And article 18.9 of UNIDO-TKL reads:

"If during the course of the tests mentioned above, any defect(s) or malfunction(s) become apparent in the plant and/or equipment supplied, or in any part of the Works, the CONTRACTOR shall immediately take

steps to *replace* the defective equipment and/or rectify the defective part of the Works in the minimum time . . ."

86. The FIDIC-EMW Conditions also provide for the situation where a second test proves not successful:

Clause 29.6: "If the Works or any Section thereof shall fail to pass the tests on the repetition thereof under Sub-Clause 5 of this Clause the Engineer shall be entitled:

"(a) To order a further repetition of the tests under the conditions of Sub-Clause 5, or

"(b) To reject the Works or Section thereof in accordance with Clause 28 (Defects before taking-over) if the results of the tests show that the Works or the Section fail to meet the performance guarantees or the agreed tolerances specified in the Contract, or if there are no such guarantees or tolerances, the results show that the Works or the Section are not in accordance with the Contract, or

"(c) To issue a Taking-Over Certificate, if the Employer so wishes, subject to such reduction of the Contract Sum as may be provided in the Contract or, failing such provision, as may be agreed by the Employer and the Contractor or, failing agreement, as may be determined by arbitration."

87. Sometimes the parties limit the number of tests and also the period within which the tests have to be repeated. An example is article 26.10.1 of UNIDO-TKL:

"Subject to the provisions of Article 26.10.2 this ninety (90) day period shall be extended if the Plant(s) is unable to operate normally and in the event of failure of this test the CONTRACTOR shall be permitted not more than two (2) other tests to be run within six (6) months immediately thereafter . . ."

88. So far we were concerned with unsuccessful tests where the contractor is responsible. Article 26.12 of UNIDO-TKL deals with interruption of performance tests:

"If the ten (10) days capacity Performance Test(s) is interrupted due to reasons for which the CONTRACTOR is not responsible, the Plant(s) shall be started again as soon as possible and when the Plant(s) has reached normal operating conditions, the Test(s) shall continue immediately thereafter. The duration of the Test(s) shall be extended by the duration of such interruptions and the Test(s) shall then be deemed to have been performed continuously . . ."

#### 7. Protocol on performance test

89. Generally for each test a protocol is signed by both parties. The FIDIC-EMW Conditions make pro-

vision where the purchaser's engineer is not represented at the tests:

*Clause 29.2:* "If the Engineer fails to appoint a time after having been asked so to do or to attend at any time or place duly appointed for making the said tests the Contractor shall be entitled to proceed in his absence and the said tests shall be deemed to have been made in the presence of the Engineer and the results of the tests shall be accepted as accurate."

90. In contrast to ECE and FIDIC, the UNIDO models are very specific in regard to protocols of any tests. For example, in UNIDO-TKL we find a construction completion report, a mechanical completion report and a performance test report.

The relevant provisions read as follows:

*Article 18.4:* "Upon satisfactory inspection of the plant and/or equipment and/or section of a Plant, the CONTRACTOR and the PURCHASER shall sign the Construction Completion Report stating that the Plant or part thereof has been inspected and is substantially complete and that any procedures required to prove the mechanical fitness and demonstration of Mechanical Guarantees prior to the Plant being put into operation may safely be carried out. (Such Construction Completion Report may include a note of any minor items which can be completed after start-up.)"

*Article 18.7:* "... When all such operations and tests have been fully and satisfactorily completed individually and/or together ... and the Mechanical Completion of the Works has been achieved, the CONTRACTOR shall thereupon prepare a Mechanical Completion Report which shall be signed by both parties following a joint examination of the Plant(s) or those sections of Utilities and Off-sites concerned, and upon such signature of such Report by both parties, the Mechanical Completion of the Plants or sections of Utilities and Off-sites concerned shall be deemed to be achieved."

*Article 26.13:* "After the successful completion of any Performance Test, in accordance with the Contract (which the PURCHASER and CONTRACTOR accept as being a successful test) the CONTRACTOR shall prepare a Performance Test Report which shall be signed by the CONTRACTOR and submitted to the PURCHASER for approval."

## IX. COMPLETION

### A. Definition of completion

91. It is not always clear what is meant by "completion". This notion is sometimes used to describe the end of the contractor's obligations to supply and con-

struct a plant, including the performance tests and the handing over of the plant. Actually it is *this time* of completion which has effect for the purchaser. This notion seems to be adopted in the ECE and FIDIC General Conditions.

92. On the other hand, completion in the UNIDO model contracts occurs before commissioning, start-up, performance tests and take-over. Article 18.2 of UNIDO-TKL provides:

"The Work(s) and/or sections and/or parts thereof shall be considered to have been completed when the requirements of Articles 18.4 to 18.7 have been satisfied ..."

Those articles relate to the construction completion (articles 18.4 and 18.5) and to the mechanical completion (articles 18.6 and 18.7).

93. Thus for the UNIDO-TKL the operation of the plant *follows* the completion:

*Article 18.10:* "Upon Mechanical Completion of any Plant and testing of each Plant in accordance with Article 18.7 and Annexure XX, as soon as possible thereafter, the relevant Plant shall be brought into operation."

94. The UNIDO-TKL also uses the notion "commercial production" describing a stage *after* completion but *before* performance tests and take-over:

*Article 18.11:* "Thereafter the Plant shall be started up and when all sections of the Plants are in a satisfactory operating state, and specification grade Ammonia and Urea are in continuous and uninterrupted production for ( ) days at ( )% capacity in accordance with the terms of the Contract, then, the Plant shall be deemed to be in Commercial Production."

### B. Time for completion

#### 1. Agreed time

95. One of the essential elements in a works contract is the time when the plant is completed and ready for operation by the purchaser. The parties therefore usually fix a date or a period for completion. If the parties choose a period they should agree on its starting point.

96. ECE 188A/574A provide for three different situations, a fixed completion period, an estimated period, and no specific period mentioned:

*Clause 20.1:* "Unless otherwise agreed the completion period shall run from the latest of the following dates:

"(a) The date of the formation of the Contract as defined in Clause 2;

"(b) The date on which the Contractor receives notice of the issue of a valid import licence where such is necessary for the execution of the Contract;

"(c) The date of the receipt by the Contractor of such payment in advance of manufacture as is stipulated in the Contract."

*Clause 20.4:* "If the time for completion mentioned in the Contract is an estimate only, either party may after the expiration of two thirds of such estimated time require the other party in writing to agree a fixed time.

"Where no time for completion is mentioned in the Contract, this course shall be open to either party after the expiration of nine months from the formation of the Contract.

"If in either case the parties fail to agree, either party may have recourse to arbitration, in accordance with the provisions of Clause 28, to determine a reasonable time for completion and the time so determined shall be deemed to be the fixed time for completion provided for in the Contract and paragraph 3 hereof shall apply accordingly."

97. In most cases it will be in the interest of the purchaser that the plant should be completed as early as possible. To encourage early completion the parties may agree on a premium.

Clause 13.3 of the FIDIC-EMW for instance contains the following provision:

"If the Contract provides for the payment of a bonus in relation to the Completion of the Works or any Section thereof this shall be set out in Part II."

98. UNIDO-TKL urges expeditious completion:

*Article 18.1:* "The CONTRACTOR shall execute the work diligently and shall adhere strictly to the requirements for expeditious completion of the Works, notwithstanding the contractual time schedules provided herein."

99. Furthermore, the above model employs a concept which is strongly opposed by contractors:

*Article 11.1:* "Time shall be deemed to be of the essence of the Contract."

*Article 11.2:* "The CONTRACTOR acknowledges and agrees that it is capable of completing its contractual obligations within the time schedules set forth in this Contract, and that it possesses the necessary skills and means to discharge its responsibilities in a proper, efficient and expeditious manner."

*Article 11.3:* "The CONTRACTOR agrees that the timely completion of the Works herein (by virtue of this Turn-Key Contract) is an integral part of the responsibilities assumed by the parties to this Contract, and accordingly, the CONTRACTOR agrees to

adhere strictly to the contractual requirements of time and promises to fulfil its contractual obligations speedily, competently and reliably."

## 2. Extension of time

100. As every construction of a plant is an individual work it is not always possible to take into account all subsequent events and meet all the time schedules. Contracts therefore usually contain provisions on extension of time.

101. Clause 20.2 of both ECE 188A/574A provides:

"Should delay in completion be caused by any of the circumstances mentioned in Clause 25 or by an act or omission of the Purchaser and whether such cause occur before or after the time or extended time for completion, there shall be granted subject to the provisions of paragraph 5 hereof such extension of the completion period as is reasonable having regard to all the circumstances of the case."

102. The FIDIC-EMW Conditions contain similar provisions, listing eight different reasons for extending the time all of which, as in the case of ECE, do not include the fault of the contractor:

*Clause 30:* "If by reason of:

"(a) Extra or additional work, or

"(b) Exceptional adverse weather conditions unforeseen at the time the Contract was signed, or

"(c) Employer's instructions beyond those specified in this Contract, or

"(d) The failure of the Employer to obtain any required import licence or permit, or the failure of the Employer to fulfil any of his obligations under the Contract, or

"(e) Delay by any other contractor engaged by the Employer, or

"(f) Any suspension of the Works under Clause 27, or

"(g) Any industrial dispute, or

"(h) Any cause, except as may otherwise be provided in the Contract, beyond the reasonable control of the Contractor,

"the Contractor shall have been delayed or impeded in the completion of the Works, whether such delay or impediment occur before or after the time or extended time fixed for completion, provided that the Contractor shall without delay have given to the Employer or the Engineer notice in writing of his claim for an extension of time, the Engineer shall on receipt of such notice and supporting detailed particulars of the claim grant the Contractor from time to time in writing either prospectively or retrospectively such extension of the time fixed by the Contract for the completion of



the Works as may be justified. Any delay on the part of a Sub-Contractor which prevents the Contractor from completing the Works within the time fixed by the Contract for the completion of the Works shall entitle the Contractor to an extension thereof if such delay was due to any cause for which the Contractor himself would have been entitled to an extension of time under this Clause."

103. The UNIDO-TKL does not deal with any possible extension but states in article 11.4:

"The CONTRACTOR acknowledges and agrees that the supply of the plant, equipment, materials and spare parts (together with the services related thereto) is crucial to the schedules for completion of the Works, and the CONTRACTOR hereby obligates itself and ensures that its scope of supply and services provided under this Contract are in conformity with the requirements of the contractual time-schedule(s) (expressly or impliedly), and, shall furthermore, in anticipation of any delay or shortfall in the scope of its supply and/or services undertake steps forthwith to remedy the delay and/or (in consultation with the PURCHASER) utilize alternate resources immediately available without compromising any of the contractual criteria as to quality and/or quantity with respect to such goods and services."

### C. Delayed completion

104. The effects of and remedies for delay are dealt with, in part two, XI, *Delays and Remedies, infra*. Here it suffices to note that there cannot be an indefinite delay and therefore, in some contracts, the purchaser is entitled to fix a final date for completion. Clause 20.5 of both ECE 188A and 574A provides:

"If any portion of the Works . . . remains uncompleted, the Purchaser may by notice in writing to the Contractor require him to complete and by such last mentioned notice fix a final time for completion which shall be reasonable taking into account such delay as has already occurred . . ."

## X. TAKE-OVER AND ACCEPTANCE

### A. General remarks

105. Take-over generally involves the taking of possession. Acceptance signifies approval. One of the main obligations of the purchaser under the Sales Convention is to "take delivery" of the goods (article 53). This obligation involves doing all acts which could reasonably be expected of him in order to enable the

seller to make delivery and taking over the goods (article 60).

106. In a works contract the obligation of the purchaser to take over the works is not always defined. In some cases take-over is regarded as identical with acceptance. In other cases the actual take-over is preceded by an acceptance (which in turn is preceded by acceptance or taking-over tests (see VIII, *Inspection and Tests, supra*). Sometimes the acceptance follows the take-over.

107. The obligation of the purchaser to take over or accept is not always spelt out but may be implied from the provisions in the contract.

### B. Pre-conditions for take-over and acceptance

108. Provision is made in ECE 188A and 574A for the taking-over of the works:

#### Clause 22. "Taking-Over"

"22.1 As soon as the Works have been completed in accordance with the Contract and have passed all the taking-over tests to be made on completion of erection, the Purchaser shall be deemed to have taken over the Works and the Guarantee Period shall start to run . . ."

109. In this context taking-over is identical with acceptance in the sense of approval (see also part two, XV, *Guarantees and Warranties, infra*). It is not even necessary for the purchaser to take-over actually, but he is deemed as having taken over if two pre-conditions are satisfied:

(a) The works have been completed (see IX, *Completion, supra*); and

(b) The works have passed all the taking-over tests (see VIII, *Inspection and Tests, supra*).

110. These pre-conditions are generally found in all contracts. The provision in FIDIC-EMW is as follows:

#### "Taking-Over"

Clause 32.1: "As soon as the Works have been completed in accordance with the Contract (except in minor respects that do not affect their use for the purpose for which they are intended and save for the obligations of the Contractor under Clause 33 (Defects) and have passed the Tests on Completion, the Engineer shall issue a certificate to the Contractor, with a copy to the Employer, (herein called a "Taking-Over Certificate") in which he shall certify the date on which the Works have been so completed and have passed the said tests, and the Employer shall be deemed to have taken over the Works on the date so certified whereupon title to and risk of loss or damage to the Works or any Section or Portion thereof shall,

subject to the provisions of Clause 15 (Liability for Accidents and Damage) and Clause 33 (Defects), pass to the Employer, but the issue of a Taking-Over Certificate shall not operate as an admission that the Works have been completed in every respect."

111. In the draft UNIDO model forms there are two types of acceptance, i.e. provisional and final. The pre-conditions for the provisional acceptance in the various models are:

	TKL 18.14	STC 18.26	CRC 18.14
(a) All certificates of inspection and all certificates of materials have been provided;	X	X	X
(b) Statement for mechanical guarantee period has been given and approved by engineer;	X	X	
(c) All documentation including drawings listed in an annex has been provided;	X	X	X
(d) Civil construction completion report has been obtained;	X		
(e) Tests have been successfully completed;	X	X	
(f) Mechanical completion report has been signed;	X		X
(g) Performance test's certificate has been submitted and accepted;	X	X	X
(h) Management services have been discharged.	X		

112. The UNIDO-CRC counter-proposal also draws the distinction between provisional and final acceptance. It proposes, however, only three pre-conditions for the issuance of the provisional acceptance certificate (article 18.11):

- (a) All certificates of inspection and of materials have been provided;
- (b) All documentation according to the annex have been provided;
- (c) The performance test certificate has been submitted by the contractor and signed by the purchaser.

113. In the UNIDO models the purchaser must issue a final acceptance certificate when all the contractual requirements have been satisfactorily complied with within twelve months of the provisional acceptance of the plant (article 18.20 of UNIDO-TKL and UNIDO-CRC, and article 18.32 of UNIDO-STC).

114. The UNIDO-CRC counter-proposal has a different conception. Here the provisional acceptance becomes the final acceptance if there are no reservations stated by the purchaser in the provisional acceptance certificate. If reservations are stated in the provisional acceptance certificate the plant will be deemed to be finally accepted when all the reservations have been

satisfactorily complied with. The purchaser will then issue, without delay, the corresponding final acceptance certificate (article 18.13 of the counter-proposal). In addition there is a time limit for the latest date of final acceptance which will start to run from the effective date of the contract.

115. The above provisions show that the completion of the plant in accordance with the contract and the successful demonstration of the tests are the minimal requirements for acceptance. In the ECE and the FIDIC Conditions there is no distinction between provisional and final acceptance.

### C. Act of acceptance

116. In many contracts take-over and acceptance are formal acts. Sometimes representatives of both parties watch the tests or jointly examine the plant. They may also agree on the necessary modifications or rectifications. Both parties sign an acceptance protocol or record stating that the plant has been delivered and accepted. If the plant comprises many single machines and equipment that have been tested individually there will be a collection of protocols of tests. The date of the signing of the last one will be the acceptance date.

117. In other cases no distinction is made between the successful performance test and the acceptance. The signing of the record of the last successful performance test is perhaps deemed to be the acceptance of the plant.

118. The ECE Guide does not deal with acceptance as a formal act. It deals with successful acceptance tests as indicating the overall completion of the plant only in relation to delay and possible calculation of penalties (paragraph 40 (ii)).

119. The FIDIC-CEC Conditions do not deal with acceptance as such. No formal act of acceptance is provided for but after completion of the work (or any substantial part thereof) the contractor may request the certificate of completion and after a certain period, which in these Conditions is called the period of maintenance, a maintenance certificate has to be issued. That will constitute approval of the works (clause 61 of FIDIC-CEC).

120. As stated earlier one of the main pre-conditions for the provisional acceptance in the UNIDO-TKL draft is the submitting and accepting of the performance test report (see also VIII, *Inspection and Tests, supra*). For the acceptance of the plant itself a special certificate will be issued according to article 26.13.1 of UNIDO-TKL:

"If the said Report (the performance test report) is satisfactory, the PURCHASER shall issue within thirty (30) days from the receipt of the CONTRACTOR's Report an *Acceptance Certificate* or shall inform the CONTRACTOR's Site representative

within the same period the reasons for non-acceptance."

#### D. *Acceptance of part of works*

121. Acceptance of part of the works is possible if different parts of the plant are ready at different times and if it is possible to use them independently. FIDIC-EMW contains two provisions concerning taking-over portions:

*Clause 32.1:* "In the event of the Works being divided by the Contract into two or more Sections the Employer shall be entitled to take over any Section or Sections before the other or others, and thereupon the Engineer shall issue a Taking-Over Certificate in respect thereof."

*Clause 32.2:* "If by agreement between the Employer, the Engineer and the Contractor any Portion of the Works (other than a Section or Sections) shall be taken over before the remainder of the Works the Engineer shall issue a Taking-Over Certificate in respect of that Portion."

#### E. *Presumed acceptance*

122. There are cases where the purchaser is deemed to have accepted the works or the plant. The following provide some examples:

##### (a) *Purchaser's failure to perform certain acts*

The purchaser is under an obligation to take delivery. This involves doing all necessary acts to enable the contractor to deliver. If, for instance, the performance tests cannot be carried out because the purchaser did not fulfil his obligations relating to material, water, energy, workers, etc., the purchaser usually is deemed as having accepted the plant.

##### (b) *Unwillingness of purchaser to have taking-over tests performed*

Clause 22.2 of both ECE 188A/574A provides as follows:

"If the Purchaser is unwilling to have the taking-over tests carried out the Works shall be deemed to have been taken over and the Guarantee Period shall start to run on a written notice to that effect being given by the Contractor."

FIDIC-EMW deals with a similar situation:

*Clause 32.4:* "If, by reason of any act or omission of the Employer or the Engineer, or of some other contractor employed by the Employer, the Contractor shall be prevented from carrying out the Tests on Completion then unless in the meantime the Works

shall have been proved not to be substantially in accordance with the Contract, the Employer shall be deemed to have taken over the Works and the Engineer shall issue a Taking-Over Certificate accordingly; . . ."

##### (c) *Postponement of take-over tests*

Clause 22.3 of both ECE 188A/574A provides that:

"If by reason of difficulties encountered by the Purchaser (whether or not covered by Clause 25), it becomes impossible to proceed to the taking-over tests, these shall be postponed for a period not exceeding six months, or such other period as the parties agree, and the following provisions shall apply:

"(a) The Purchaser shall make payments as if the taking-over had taken place, . . .

"(f) If at the end of six months or such other period as the Parties may have agreed the tests have not taken place, the provisions of paragraph 22.2 shall apply unless the provisions of Clause 25 are applicable."

##### (d) *Purchaser's conduct*

Apart from the performance tests there are other cases where the purchaser is deemed to have accepted the plant. Clause 32.1 of FIDIC-EMW provides:

"Save as provided in Sub-Clause 3 of this Clause the Employer shall not use the Works or any Section or Portion thereof until a Taking-Over Certificate has been issued in respect thereof. If nevertheless, the Employer does so use the Works or any Section or Portion thereof the Works or Section or Portion shall be deemed to have been taken over."

##### (e) *Delay in acceptance*

The UNIDO-TKL draft also contains a provision concerning a presumed acceptance. According to article 26.13.2 the non-issuance of the acceptance certificate mentioned earlier does not in all cases prevent the acceptance:

". . . in the event of the PURCHASER failing to issue the Acceptance Certificate or to inform the CONTRACTOR as provided in Article 26.13.1, the CONTRACTOR shall request the PURCHASER for an explanation for the delay and if the PURCHASER fails to respond within another thirty (30) days the Acceptance of the Plant for which the Performance Test was conducted shall be deemed to have taken place, on the date that the test was successfully completed."

#### F. *Refusal of acceptance*

123. It follows from the foregoing that the purchaser may refuse to accept the works if the plant has not been

constructed in accordance with the contract or if the plant is not complete or if the tests have not been successfully carried out. However, the purchaser has to accept if there are only minor or immaterial defects (see clause 32.1 FIDIC-EMW, *supra*, paragraph 121).

124. In the UNIDO models minor defects do not permit the purchaser to refuse acceptance. This is not stated in the drafts but it follows from other provisions. It seems that the provisional acceptance certificate will be issued even if:

(a) The tests are not successful and the purchaser claims liquidated damages (article 18.17 of UNIDO-TKL);

(b) Repairs are necessary which the contractor has to carry out (article 18.18 of UNIDO-TKL).

#### G. Legal effects of take-over and acceptance

125. By accepting the plant the purchaser acknowledges that the contract has been duly performed. However, the parties may state in the acceptance protocol the defects, if any, and agree on the period for their rectification.

126. According to clause 32.1 of FIDIC-EMW "the issue of a Taking-Over Certificate shall not operate as an admission that the Works have been completed in every respect."

127. A similar provision is contained in both UNIDO-TKL and UNIDO-CRC:

*Article 18.16:* "The Provisional Acceptance of the Plant or the Take-Over of any specified part or section of the Plant(s) by the PURCHASER . . . shall not be construed as evidence that any portions of the Work(s), part(s), section(s) and/or material(s) thereof are complete."

Similarly in UNIDO-STC:

*Article 18.28:* "The Provisional Acceptance of the Plant(s) or the Take-Over of any specified part or section of the Plant(s) by the PURCHASER shall not in any way release the CONTRACTOR from his obligations under the terms of this Contract, and shall not be construed as evidence that the Plant(s) are free of defects."

128. An international group of contractors has criticized those provisions, stating that a signed report must mean what it says and any reservations thereon should be written into the report (see ID/WG.318/4, page 23).

129. According to clause 32.1 of FIDIC-EMW the legal effect of the acceptance and take-over is that title to and risk of loss or damage to the works pass to the purchaser.

130. According to clause 22.1 of both ECE 188A/574A the guarantee period commences on the date of acceptance.

131. According to article 18.19 of UNIDO-TKL the purchaser, upon take-over, "shall be responsible for the management, operation and maintenance of the Work(s), and shall take out and carry such insurances as may be deemed necessary."

132. Sometimes the credit period, payment of installments or payment of interests commences on the date of acceptance. However, this effect is sometimes expressly excluded. For instance, according to clause 62 (1) of FIDIC-CEC, the maintenance certificate which marks the approval or acceptance of the works is not a condition precedent to payment to the contractor.

133. On the other hand according to article 26.15 of UNIDO-TKL the acceptance certificate entitles the contractor to receive payment:

"The issue of these Provisional Acceptance Certificates shall . . . entitle the CONTRACTOR to receive due payments on completion of the Performance Guarantees and Acceptance of the Plant in accordance with Article 20."

[A/CN.9/WG.V/WP.4/Add.4\*]

## XI. DELAYS AND REMEDIES

### A. Preliminary remarks

1. As a general rule, the parties to a contract must perform the contract according to its terms. This obligation relates not only to the performance itself but also to the time within which the performance must be completed. If the party does not perform within the time fixed by the contract, there exists a "delay" under the terms of the contract.

2. Delays in the execution of a contract may occur at different stages of the contract and can be caused by a breach of the contract by the parties or may be attributable to causes beyond the control of the parties.

3. If a delay occurs the aggrieved party may ask that this situation be remedied. The remedy will depend on the gravity and the seriousness of the delay. In view of the nature of contracts for the supply and construction of large industrial works, it is to be expected that they will be essentially performance oriented and that it will be only as a measure of last resort that the aggrieved party will be entitled to put an end to the contract.

\* 27 May 1981.

## B. *Kinds of delays and their remedies*

### 1. *Delay in performing the main obligations*

#### (a) *Completion*

4. In the event of a delay in the completion of the works, clause 47 of FIDIC-CEC provides that:

"... the Contractor shall pay to the Employer the sum stated in the Contract as liquidated damages for such default and not as a penalty for every day or part of a day which shall elapse between the time prescribed by Clause 43 hereof and the date of certified completion of the Works..."

5. However, the same clause of FIDIC-CEC goes on further:

"The payment or deduction of such damages shall not relieve the Contractor from his obligation to complete the Works, or from any other of his obligations and liabilities under the Contract."

6. Under clause 31.1 of FIDIC-EMW, the purchaser is also entitled "to a reduction of the Contract Sum unless it can be reasonably concluded from the circumstances of the particular case that the Employer has suffered no loss." The exact amount of such reduction will be determined in accordance with the figures provided for in an appendix to the tender.

7. If the works remain uncompleted for a long period of time, clause 31.2 of FIDIC-EMW provides that:

"If any Portion of the Works in respect of which the Employer has become entitled to the maximum reduction under Sub-Clause 1 of this Clause remains uncompleted the Employer may by notice in writing to the Contractor require him to complete and by such notice fix a final time for completion which shall be reasonable having regard to such delay as has already occurred. If for any reason, other than one for which the Employer or some other contractor employed by him is responsible, the Contractor fails to complete within such time, the Employer may by further written notice to the Contractor elect either

"(a) To require the Contractor to complete, or

"(b) To terminate the Contract in respect of such Portion of the Works

"and recover from the Contractor any loss suffered by the Employer by reason of the said failure up to an amount not exceeding the sum named in the Appendix to the Tender or, if no sum is named, that part of the Contract Sum that is properly apportionable to such Portion of the Works as cannot by reason of the Contractor's failure be put to the use intended."

8. The solution envisaged by FIDIC-EMW is similar to that in the ECE General Conditions in case the delay in the completion of the works is not remedied

immediately. Clause 20.5 of both ECE 188A/574A provides that:

"If any portion of the Works in respect of which the Purchaser has become entitled to the maximum reduction provided for by paragraph 3 hereof, or in respect of which he would have been so entitled had he given the notice referred to therein, remains uncompleted, the Purchaser may by notice in writing to the Contractor require him to complete and by such last mentioned notice fix a final time for completion which shall be reasonable taking into account such delay as has already occurred. If for any cause other than one for which the Purchaser or some other Contractor employed by him is responsible, the Contractor fails to complete within such time, the Purchaser shall be entitled by notice in writing to the Contractor, and without requiring the consent of any Court, to terminate the Contract in respect of such portion of the Works and thereupon to recover from the Contractor any loss suffered by the Purchaser by reason of the failure of the Contractor as aforesaid up to an amount not exceeding the sum named in ... the Appendix, or, if no sum be named, that part of the price payable under the Contract which is properly attributable to such portion of the Works as could not in consequence of the Contractor's failure be put to the use intended."

9. The remedies for delay in completion or for non-completion are usually damages (see XII, *Damages and limitation of liability, infra*) or liquidated damages and termination (see part two, XVII, *Termination*).\*

#### (b) *Payment*

10. If the purchaser delays in making payment, clause 11.5 of both ECE 188A/574A provides that:

"the Contractor may postpone the fulfilment of his own obligations until such payment is made, unless the failure of the Purchaser is due to an act or omission of the Contractor"

11. When the delay in paying continues, clause 11.7 of both ECE 188A/574A provides that:

"... the Contractor shall on giving to the Purchaser within a reasonable time notice in writing be entitled to the payment of interest on the sum due at the rate fixed in ... the Appendix from the date on which such sum became due. If at the end of the period fixed in ... the Appendix, the Purchaser shall still have failed to pay the sum due, the Contractor shall be entitled by notice in writing to the Purchaser, and without requiring the consent of any Court, to terminate the Contract and thereupon to recover from the Purchaser the amount of his loss up to the sum mentioned in ... the Appendix."

\* A/CN.9/WG.V/WP.4/Add.7 (reproduced below).

12. Under clause 69(1) of FIDIC-CEC, the contractor may terminate the contract:

"In the event of the Employer:

"(a) Failing to pay to the Contractor the amount due under any certificate of the Engineer within thirty days after the same shall have become due under the terms of the Contract, subject to any deduction that the Employer is entitled to make under the Contract . . ."

13. The UNIDO-TKL model does not contain any provision granting the contractor remedies in the event the purchaser delays in making payment under the terms of the contract. The remedies available to the contractor in such a case would, therefore, be those existing under the applicable law.

#### (c) Taking delivery

14. If the purchaser delays in taking delivery, clause 10.1 of both ECE 188A/574A provides that "he shall nevertheless make any payment conditional on delivery as if the Plant had been delivered. The Contractor shall arrange for the storage of the Plant at the risk and cost of the Purchaser. If required by the Purchaser, the Contractor shall insure the Plant at the cost of the Purchaser . . ."

15. The FIDIC-EMW Conditions also contain similar provisions on the consequences of the purchaser's delay in taking delivery, i.e. payment, storage and insurance (clauses 26.2, 26.4, 26.5, 26.7).

### 2. Delay in performing other obligations

16. Some of the possible cases of delay and their consequences have been dealt with in other chapters and will, therefore, not be repeated here. As regards delayed tests, see part two, VIII, *Inspection and Tests*,\* for delays in curing defects, see part two, XV, *Guaranties*\*\* and XVI, *Rectification of Defects*.\*\*\*

### 3. Delays due to exonerating events

17. Certain aspects of the question are discussed in chapter XIII, *Exoneration*,\*\*\*\* which deals with events of *force majeure* or frustration and with other types of events which prevent the parties from performing the contract.

18. Some of the forms under study deal with events other than *force majeure*, frustration or exoneration that may result in delays in the performance of the contract. Such other causes for delay to which for instance clause

44 of FIDIC-CEC refers are "extra or additional work of any kind" and to "exceptional adverse climatic conditions".

19. In the event that the contractor's performance is delayed for a reason beyond the control of the parties, article 44 of FIDIC-CEC provides that the contractor is entitled "to an extension of time for the completion of the Works". The period of extension is to be determined by the engineer who "shall notify the Employer and the Contractor accordingly".

20. In order for the engineer to take account of the additional or extra work or of other special circumstances, the contractor must notify him in writing. This notice must be sent "within twenty-eight days after such work has been commenced, or such circumstances have arisen, or as soon thereafter as is practicable" and it must contain "full and detailed particulars of any extension of time to which [the Contractor] may consider himself entitled in order that such submission may be investigated at the time".

21. Article 19 of UNIDO-TKL deals with the extension of time for completion if delay is caused by circumstances beyond the control of the parties. Article 19.1 of UNIDO-TKL refers to "Vandalism, Malicious Damage and Death or Injury to essential personnel" but excludes occurrences or events covered by articles 18.18 (repairs and modifications of the plant), 29.10 (inability to prove and demonstrate the guaranty tests) and 34 (*force majeure*) which may also delay the completion of the works.

22. Under article 19.1 of UNIDO-TKL, the contractor must also make a written request to the purchaser "for a reasonable extension of time for completion of work or any portion of it to the extent that the factors affecting delay prevailed in the circumstances." This written request must be made within ten days of the occurrence specified above which resulted in the delay.

## XII. DAMAGES AND LIMITATION OF LIABILITY

### A. Introduction

23. The liability to pay damages for breach of contract is one of the most important consequences of the failure to perform. The importance appears to be particularly significant in international contracts for the supply and construction of large industrial plants because of the extent of damages that may result from the breach of such contracts. Moreover, there may be problems relating to damages presented by a guaranty. Therefore, clauses providing for damages which are to be

\* A/CN.9/WG.V/WP.4/Add.3 (reproduced above).

\*\* A/CN.9/WG.V/WP.4/Add.6 (reproduced below).

\*\*\* *Ibid.*

\*\*\*\* A/CN.9/WG.V/WP.4/Add.5 (reproduced below).

paid in case of failure to perform are often found in such contracts.

24. The limitation of liability in case of exonerating events is dealt with in chapter XIII. This chapter covers only limitations of liability in respect of the extent of damages to be paid. Such limitations may be summed up as follows:

Exclusion of unforeseeable damage,

Exclusion of indirect and consequential loss and anticipated profits,

Reduction in damages in case of failure to mitigate the loss,

Stipulation of limited amount of damages,

Exclusion of damages caused by defects of materials provided or design stipulated by the purchaser,

Exclusion of personal injury and damage to property not being the subject matter of the contract.

#### B. *Exclusion of unforeseeable damage*

25. Rules excluding from liability for loss which could not have been foreseen by a party in breach can be found in many international conventions, legal systems, as well as general conditions. In all these rules, the only relevant time is that of the conclusion of the contract. Knowledge which is subsequently acquired is not relevant to the measure of damages.

26. Article 74 of the Sales Convention reads:

"Damages for breach of contract by one party consist of a sum equal to the loss, including loss of profit, suffered by the other party as a consequence of the breach. Such damages may not exceed the loss which the party in breach foresaw or ought to have foreseen at the time of the conclusion of the contract, in the light of the facts and matters of which he then knew or ought to have known, as a possible consequence of the breach of contract."

27. Such a principle of excluding recovery of damages for unforeseeable loss is contained in clause 26.1 of both ECE 188A/574A which reads:

"Where either party is liable in damages to the other, these shall not exceed the damage which the party in default could reasonably have foreseen at the time of the formation of the contract."

28. A similar provision is contained in the FIDIC-EMW Conditions clause 16.2:

"Where either the Employer or the Contractor is liable in damages to the other these shall not exceed the damage which the party in default could reasonably have foreseen at the date of the Contract."

#### C. *Exclusion of indirect or consequential loss and anticipated profits*

29. In clause 16.1 of FIDIC-EMW indirect or consequential damage is excluded to some extent:

"Except as provided in Clause 31.1 (Delay in Completion) for a reduction of the Contract Sum for delay and except as provided in Clause 33.11 (Gross Misconduct), the Contractor shall not be liable to the Employer by way of indemnity or by reason of any breach of the Contract for loss of use (whether complete or partial) of the Works or of profit or of any contract or for any indirect or consequential damage that may be suffered by the Employer."

30. Article 30.6 of the UNIDO-TKL model contract and article 30.6 of UNIDO-CRC model contract exclude anticipated profits and consequential loss in the following manner:

"The CONTRACTOR shall not be liable under the Contract for loss of anticipated profits or for any consequential loss or damage arising from any cause, except to the extent of repaying to the PURCHASER any amount receivable under Article 24 and/or pursuant to other insurance policies held by the CONTRACTOR solely in connection with the types of losses referred to in this Article 30.6."

31. On the other hand, article 30.3 of UNIDO-CRC counter-proposal contains a broader limitation of anticipated profits and consequential loss:

"The CONTRACTOR shall not be liable, in any event, whether under the Contract, negligence, or otherwise for loss of anticipated profits, or for any consequential loss or damage arising from any cause."

#### D. *Reduction in damages in case of failure to mitigate the loss*

32. The party who relies on breach of contract is usually required by applicable legal rules or the contract to mitigate the loss resulting from the breach of contract. The purpose of such provisions is to prevent the damages from swelling.

33. Article 77 of the Sales Convention reads:

"A party who relies on a breach of contract must take such measures as are reasonable in the circumstances to mitigate the loss, including loss of profit, resulting from the breach. If he fails to take such measures, the party in breach may claim a reduction in the damages in the amount by which the loss should have been mitigated."

34. Similar provisions are contained in clause 26.2 of both ECE 188A/574A which reads:



"The party who sets up a breach of Contract shall be under a duty to take all necessary measures to mitigate the loss which has occurred provided that he can do so without unreasonable inconvenience or cost. Should he fail to do so, the party guilty of the breach may claim a reduction in the damages."

35. A similar provision is also found in clause 16.3 of FIDIC-EMW:

"In all cases the party establishing a breach of contract shall be under a duty to take all necessary measures to mitigate the loss which has occurred provided that he can do so without unreasonable inconvenience or cost. Should he fail to do so, the party in breach of the Contract may claim a reduction in the damages."

#### E. Stipulation of limited amount of damages

36. The extent of damages to be paid in case of breach of contract is often limited by the parties in the contract, either by a percentage of the price of the works or by a certain amount stipulated directly in the contract. In such a case the right to claim damages is governed by rules otherwise applicable but the right to damages cannot exceed the amount agreed upon by the parties.

37. Clause 30.5 of the UNIDO-TKL model contract provides as follows:

"The total liability of the CONTRACTOR under the Contract shall not exceed . . . % of the total Project Cost, or, (state amount) whichever is the greater, with the exception of the CONTRACTOR's unlimited liability for the fulfillment of warranties, Absolute Guarantees, modifications, rectifications and completion of the Work(s) as well as the reimbursement to the PURCHASER of any amount(s) received by the CONTRACTOR under any Insurance Policies held by the CONTRACTOR as well as through those other specifically taken out for the purposes of this Contract."

An identical provision is contained in clause 30.5 of UNIDO-CRC.

38. A similar provision is contained in clause 30.5 of UNIDO-STC. However, the limitation of liability is determined only by a percentage of the total contract price.

39. Clause 30.1 of UNIDO-CRC counter-proposal is of a more general nature:

"The overall financial liability, whether founded on Contract, negligence or otherwise, of the CONTRACTOR arising out of or in connection with the realisation of the Contract shall not exceed (. . .)% of the firm price stated in Article 20.1.1."

40. Such a limitation of damages is included in clause 16.4 of FIDIC-EMW in this way:

"The liability of the Contractor to the Employer under Clause 15 for any one act or default shall not exceed the sum stated in Part II of these Conditions, and the Contractor shall have no liability to the Employer in respect of any loss of or damage to property which shall occur after the expiration of the period stated in Part II of these Conditions."

41. International contracts for supply and construction often provide for the payment of a sum of money (penalty, liquidated damages) upon a breach of a contractual obligation. Such clauses are inserted by parties to determine, at the time of the conclusion of the contract, the damages to be paid in case of its breach, without the need of proving the extent of loss actually brought about by such a breach. At the same time, however, the agreed amount very often serves as a limitation of liability of the debtor.

42. The UNCITRAL Working Group on International Contract Practices was requested to deal with the question of liquidated damages and penalty clauses.<sup>1</sup> The Secretariat submitted two studies.<sup>2</sup> At its second session (New York, 13-17 April 1981) the Working Group adopted a draft rule on the relationship between the right to obtain the agreed sum (liquidated damages, penalty) and to claim damages for breach of the contractual obligation to which it is accessory. The rule reads:

"Unless the parties have agreed otherwise, if a failure of performance in respect of which the parties have agreed that a sum of money is to be recoverable or forfeited occurs, the creditor is entitled, in respect of the failure, to recover or forfeit the sum, and is entitled to damages to the extent of the loss not covered by the agreed sum, but only if he can prove that this loss grossly exceeds the agreed sum."<sup>3</sup>

#### F. Exclusion of damages caused by defects of materials provided or design stipulated by the purchaser

43. Contracts for the supply and construction of large industrial works sometimes stipulate that the purchaser is to provide some materials and/or design

<sup>1</sup> Report of the United Nations Commission on International Trade Law on the work of its twelfth session (1979), *Official Records of the General Assembly, Thirty-fourth Session, Supplement No. 17* (A/34/17), para. 31 (Yearbook . . . 1979, part one, II, A).

<sup>2</sup> Report of the Secretary-General entitled "Liquidated damages and penalty clauses" (A/CN.9/196) (reproduced in this volume, part two, II, A) and Report of the Secretary-General entitled "Liquidated damages and penalty clauses (II)" (A/CN.9/WG.2/WP.33 and Add.1) (reproduced in this volume, part two, I, B).

<sup>3</sup> Report of the Working Group on International Contract Practices on the work of its second session (A/CN.9/197), para. 52 (reproduced in this volume, part two, I, A).

needed for the production of the plant or construction of the works. In such cases the contracts usually exclude responsibility of the contractor for defects caused by such materials or designs. The exclusion of liability covers the curing of defects as well as damages concerning loss brought about by such defects.

44. Clause 23.12 of both ECE 188A/574A reads:

"The Contractor's liability does not apply to defects arising out of materials provided, or out of a design stipulated, by the Purchaser."

45. A similar principle follows from clause 33.2 of the FIDIC-EMW Conditions:

"The Contractor shall be responsible for making good with all possible speed at his expense any defect in or damage to any portion of the Works which may appear or occur during the Defects Liability Period and which arises either:

"(a) From any defective materials, workmanship or design (other than a design made, furnished or specified by the Employer and for which the Contractor has disclaimed responsibility in writing within a reasonable time after receipt of the Employer's instructions), or . . ."

*G. Exclusion of personal injury and damage to property not being the subject-matter of the contract*

46. In many contracts for the supply and construction of large industrial plants there is express provision excluding personal injury and damage to property not being the subject matter of the contract. Such injury or damages may be governed, however, by applicable legal rules of a mandatory nature.

47. The sphere of application of the Sales Convention is limited in this respect in article 5 which reads:

"This Convention does not apply to the liability of the seller for death or personal injury caused by the goods to any person."

48. Contracts for the supply and construction of large industrial plants cannot, of course, disentitle third persons not being parties to such a contract. Some general conditions, however, deal with the responsibility of the contractor in relationship to the purchaser in case of such damage. Clause 23.14 of both ECE 188A/574A provides:

"After taking over and save as in this Clause expressed, the Contractor shall be under no liability even in respect of defects due to causes existing before taking over. It is expressly agreed that the Purchaser shall have no claim in respect of personal injury or of damage to property not the subject-matter of the Contract arising after taking over nor for loss of profit unless it is shown from the circumstances of the case

that the Contractor has been guilty of gross misconduct."

49. According to clause 23.15 of both ECE 188A/574A:

"'Gross misconduct' does not comprise any and every lack of proper care or skill, but means an act or omission on the part of the Contractor implying either a failure to pay due regard to serious consequences which a conscientious Contractor would normally foresee as likely to ensue, or a deliberate disregard of any consequences of such act or omission."

50. Liability for personal injury or damage to property occurring before all the works have been taken over is dealt with in clause 24.1 of both ECE 188A/574A.

51. Clause 15.5 of FIDIC-EMW reads:

"If there shall occur, after the commencement of the Defects Liability Period in respect of any Section or Portion of the Works, any loss of or damage or injury to any property (other than property forming part of the Works not yet taken over) or person as a result of a cause occurring prior to the commencement of the Defects Liability Period the Contractor's liability, subject to Clause 16.4 (Limitation of Liability), shall be as follows:

" . . .

"(b) In respect of damage or injury to any property or to any person and of any actions, claims, demands, costs, charges and expenses arising in connection therewith, the Contractor shall be liable to the extent that such damage or injury was caused by the negligence of the Contractor or a Sub-Contractor or by defective design (other than a design made, furnished or specified by the Employer and for which the Contractor has disclaimed responsibility in writing within a reasonable time after receipt of the Employer's instructions) materials or workmanship but not otherwise."

52. A more general rule is contained in clause 22 of FIDIC-CEC:

"(1) The Contractor shall, except if and so far as the Contract provides otherwise, indemnify the Employer against all losses and claims in respect of injuries or damage to any person or material or physical damage to any property whatsoever which may arise out of or in consequence of the execution and maintenance of the Works and against all claims, proceedings, damages, costs, charges and expenses whatsoever in respect of or in relation thereto except any compensation or damages for or with respect to:

"(a) The permanent use or occupation of land by the Works or any part thereof.

"(b) The right of the Employer to execute the Works or any part thereof on, over, under, in or through any land.

"(c) Injuries or damage to persons or property which are the unavoidable result of the execution or maintenance of the Works in accordance with the Contract.

"(d) Injuries or damage to persons or property resulting from any act or neglect of the Employer, his agents, servants or other contractors, not being employed by the Contractor, or for or in respect of any claims, proceedings, damages, costs, charges and expenses in respect thereof or in relation thereto or where the injury or damage was contributed to by the Contractor, his servants or agents such part of the compensation as may be just and equitable having regard to the extent of the responsibility of the Employer, his servants or agents or other contractors for the damage or injury.

[A/CN.9/WG.V/WP.4/Add.5\*]

### XIII. EXONERATION

#### A. Introduction

1. Most, if not all, legal systems make provision for unforeseen or unavoidable circumstances which prevent, impede or delay the performance of a contract. The nature and scope of such circumstances affecting a contract differ in varying degrees among different legal systems. The two main doctrines that have been evolved to deal with such circumstances are *force majeure* and frustration, though the former doctrine may mean different things in different legal systems.

2. Parties often insert "*force majeure*" or "frustration" clauses either to expand or narrow the scope of the two doctrines. In such clauses, parties may also allocate their risks in a more precise manner taking into consideration the nature of the performance of the particular contract.

3. In this study, the term "exoneration" is used to cover circumstances relieving parties from liability. Although the circumstances under discussion may straddle the doctrines of *force majeure* or frustration the term "exoneration" is used to avoid confusion, as there may be events under consideration which do not fall within the scope of either one or the other of the two doctrines as understood in the various legal systems.

However, the terms "*force majeure*", "frustration" and other epithets will be used where clauses under discussion are taken from contexts which employ these terms.

4. An exoneration clause constitutes one of the most important clauses in a works contract; it deals essentially with the allocation of risks in the event of changed circumstances. Such a clause could save the contract from automatic termination which may be too drastic and may not be to the mutual interests of both parties. At a regional level, attempts at drafting "relief" clauses for use in contracts for the supply and erection of plant and machinery have been made, for example, by ECE. The ECE General Conditions are designed for application in different legal systems. At a global level, the "Exemptions" provision in the Sales Convention provides an example of success in the harmonization of this area of law in the context of sale of goods. Parties to works contracts have also attempted to modify the doctrines of *force majeure* and frustration in order to determine the kinds of contingency that would suspend or terminate their obligations and also the consequences of such suspension or termination.

#### B. Exonerating circumstances

##### 1. Force majeure clauses in contractual stipulations

5. An examination of some works contracts indicates a number of approaches:

(a) Reference is made to the applicable law of the contract with no attempt to extend or narrow its scope. For example, in one clause reference was made to "Articles 513 and 514 of the Civil Code".

(b) *Force majeure* clauses are defined generally by the parties but no attempt is made in spelling out the exonerating events. For example, one such clause reads: "Neither party hereto shall be liable for any failure or delay in performing any obligation hereunder (except the payment of any amount due hereunder) due to *causes which are reasonably beyond its control*." This clause is from one of the contracts to be performed in Trinidad and Tobago. The clause is to be read with the applicable law of the contract.

(c) Some *force majeure* clauses attempt to list, in varying details, the exonerating circumstances. But most are only illustrative of the scope and leave the question to be determined by the judge or arbitrator. Other clauses attempt a more comprehensive, though not exhaustive, list and end with a general clause, as for example, that it is "... without prejudice to the generality, any other circumstance or occurrence beyond the reasonable control of the sellers."

6. The following criteria were found in the definition of "*force majeure*" or other such-like clauses but with varying combinations:

\* 17 March 1981.

Unexpected circumstances  
 Foreseen but unavoidable event  
 Unforeseen event  
 Cause beyond the control of the parties  
 Prevented from fulfilling obligations  
 Unable to prevent despite exercise of reasonable care and due diligence  
 Event occurring after conclusion of contract  
 Event not due to fault of party.

7. Subject to variations as to scope and precision, the following are some exonerating circumstances found in *force majeure* clauses:

Natural disasters (e.g. lightning, earthquakes, storms, floods)  
 Political obstacles (e.g. acts of enemy, revolutions, riots, sabotage, embargoes, withdrawal of licences)  
 Economic obstacles (e.g. withdrawal of licences, embargoes, industrial disputes, strikes, lock-outs, industrial disturbances, shortage of labour, concerted acts of workmen)  
 Legal obstacles (e.g. acts of government)  
 Transport obstacles (e.g. delay of vessel, shipwreck)  
 Other obstacles (e.g. explosions, breakdown of machinery, accidents, theft).

## 2. ECE 188A and ECE 574A

8. Clause 25.1 of ECE 188A reads:

"The following shall be considered as cases of relief if they intervene after the formation of the Contract and impede its performance: industrial disputes and any other circumstances (e.g. fire, mobilization, requisition, embargo, currency restrictions, insurrection, shortage of transport, general shortage of materials and restrictions in the use of power) when such other circumstances are beyond the control of the parties."

9. Clause 25.1 of ECE 574A reads:

"Any circumstances beyond the control of the parties intervening after the formation of the Contract and impeding its reasonable performance shall be considered as cases of relief. For the purposes of this Clause circumstances not due to the fault of the party invoking them shall be deemed to be beyond the control of the parties."

10. The difference between ECE 188A and ECE 574A is that the former contains some specific references to the kinds of relief which fall within its scope. The enumeration under 188A is not exhaustive but only illustrative of some of the "reliefs" contemplated.

11. Under both clauses the circumstances must occur after the formation of the contract and must be beyond the control of the parties. There must be a nexus between the supervening circumstances and the performance of the contract. ECE 188A speaks of circumstances which "impede its performance" while ECE 574A, "impeding its *reasonable* performance". The epithet "reasonable" qualifying "performance" was thought sufficient to exclude strikes and industrial disputes which may impede performance, but may not be "reasonable", depending of course on the nature of the strike and industrial dispute.

## 3. FIDIC-CEC

12. A works contract would invariably involve some civil engineering works. The provision on "frustration" in FIDIC-CEC reads:

*Clause 66:* "If a war, or other circumstances outside the control of both parties, arises after the Contract is made so that either party is prevented from fulfilling his contractual obligations, or under the law governing the Contract, the parties are released from further performance, then the sum payable by the Employer to the Contractor in respect of the work executed shall be the same as that which would have been payable under Clause 65 hereof if the Contract had been terminated under the provisions of Clause 65 hereof."

13. Two categories of "frustration" are provided in the above clause: first, "circumstances outside the control of both parties" ("war" being an example) which prevent the fulfilling of contractual obligations; secondly, where the governing law releases the parties from further performance.

14. In addition, the FIDIC-CEC Conditions contain an enumeration of "special risks" in clause 65 (5). These risks may subsequently lead to the "frustration" of the contract within the meaning of clause 66:

"The special risks of war, hostilities (whether war be declared or not), invasion, act of foreign enemies, the nuclear and pressure waves risk described in Clause 20 (2) hereof, or insofar as it relates to the country in which the Works are being or are to be executed or maintained, rebellion, revolution, insurrection, military or usurped power, civil war, or unless solely restricted to the employees of the Contractor or of his Sub-Contractors and arising from the conduct of the Works, riot, commotion or disorder."

## 4. FIDIC-EMW

15. All works contracts would invariably involve some electrical and mechanical works. A clause on "frustration" is contained in FIDIC-EMW:

*Clause 48:* "If a war or other circumstance outside the control of both parties arises after the

Contract is made so that under the law governing the Contract the parties are released from further performance then the sum payable by the Employer to the Contractor in respect of the work executed shall be the same as that which would have been payable under Clause 46 if the Contract had been terminated under the provisions of Clause 46."

16. This clause is similar to the FIDIC-CEC clause (see *supra*, paragraph 12). However, it leaves the question of "frustration" to be determined by reference only to the law governing the contract.

17. The "special risks" defined in FIDIC-EMW are similar though not identical to FIDIC-CEC (see *supra*, paragraph 14). Clause 47.5 of the former reads:

"The special risks are the nuclear and pressure wave risks described in Clause 15.1 (b) iii and IV or insofar as it relates to the country in which the Works are to be erected, war, hostilities (whether war be declared or not), invasion, act of foreign enemies, rebellion, revolution, insurrection, military or usurped power, civil war or, unless solely restricted to the employees of the Contractor or of his Sub-Contractor and arising from the conduct of the Works, riot, commotion or disorder."

In FIDIC-EMW, except for nuclear and pressure wave risks, all other risks so enumerated in the above clause must relate to the country in which the works are carried out. These include war, hostilities (whether declared or not) and invasion. However, in FIDIC-CEC, risks of war, hostilities and invasion need not relate to the country in which the works are carried out.

#### 5. UNIDO model contracts (CRC, TKL and STC)

18. All the three UNIDO model contracts adopt the same approach to the definition of *force majeure*. For convenience, reference is made to clause 34.1 of the UNIDO-CRC model contract:

"In this Contract, *Force Majeure* shall be deemed to be any cause beyond the reasonable control of the CONTRACTOR or the PURCHASER (as the case may be) which prevents, impedes or delays the due performance of the Contract by the obligated party and which, by due diligence, the affected party is unable to control, despite the making of all reasonable efforts to overcome the delay, impediment or cause."

*Force Majeure* is defined in article 34.1 to include the following:

"Any war or hostilities;

"Any riot or civil commotion;

"Any earthquake, flood, tempest, lightning, unusual weather or other natural physical disaster. Impossibility in the use of any railway, port, airport, shipping-service or other means of transportation (occurring concurrently . . .);

"Any accident, fire or explosion;

"Any strike, lock-out or concerted acts of workmen (except where it is within the power of the party involving the Force Majeure to prevent);

"Shortages or unavailability of materials (compounded by the same shortage or unavailability from alternate sources) if beyond the CONTRACTOR's control."

#### 6. Sales Convention

19. Most contracts for the supply and construction of large industrial works would probably fall outside the scope of the Sales Convention. Be that as it may, the approach adopted in the "Exemptions" provision in the Convention may be relevant in examining an exoneration clause in a works contract. Article 79 (1) reads:

"A party is not liable for a failure to perform any of his obligations if he proves that the failure was due to an impediment beyond his control and that he could not reasonably be expected to have taken the impediment into account at the time of the conclusion of the contract or to have avoided or overcome it or its consequences."

20. The conditions under which a party is not liable for a failure to perform his obligations under article 79 (1) are similar to some *force majeure* clauses in works contracts.

21. The Convention also makes provision for exemption in the case of a failure by a third party whom the seller had engaged to perform the whole or a part of the contract. Article 79 (2) is intended to be limited to the exemption of a sub-contractor and not a supplier. It reads:

"If the party's failure is due to the failure by a third person whom he has engaged to perform the whole or a part of the contract, that party is exempt from liability only if:

"(a) He is exempt under the preceding paragraph; and

"(b) The person whom he has so engaged would be so exempt if the provisions of that paragraph were applied to him."

#### 7. ICC force majeure clause

22. ICC has drafted a *force majeure* clause for insertion in "contracts to be performed by stages or with deferred performance especially in international practice". In its report on "*Force majeure* and hardship clauses in international contracts" it was stated that "it is necessary to adapt the clauses to the basic economic situation which they are to govern" (Documents Nos. 460/233, 460/247 and 460/262).

23. Among the types of contract which were examined in the preparation of the ICC *force majeure* clause were "contracts aimed at the construction of large industrial, mining, agricultural or building complexes, and particularly so-called 'turn-key contracts'".

24. The following *force majeure* clause was suggested (revised 1980):

*"Clause of release from liability"*

*"1. Definition of circumstances releasing from liability"*

*"(1) Event of force majeure"*

"A circumstance releasing a party from liability may be defined as any event of force majeure, or any unforeseen event occurring outside the control of that party, in so far as he was unable to prevent its occurrence or anticipate its effects, which temporarily or permanently prevents him from fulfilling his contractual obligations in whole or in part, account being taken of the diligence which may reasonably be required of him.

*"(2) Other circumstances"*

"A circumstance releasing a party from liability may be defined as any one of the following events, when they are of a nature to prevent one of the parties temporarily or permanently from fulfilling his obligations in whole or in part:

*"(a)* War and civil war, whether declared or not, riots and revolutions, acts of piracy, boycott;

*"(b)* Acts of sabotage, requisition, confiscation, nationalisation, embargoes and expropriation;

*"(c)* Violent storms, cyclones, earthquakes, tidal waves, destruction by lightning and other natural disasters;

*"(d)* Explosions, fires, destruction of machines, of factories, and of any kind of installations inasmuch as these occurrences are not imputable to the fault of the party relying on them;

*"(e)* Strikes and lock-outs of all kinds, including 'go-slows', occupation of factories and premises, strikes which do not involve any interruption of work, and work stoppages arising in the enterprises of one of the parties, whether or not any preliminary conciliation procedure laid down by law has been followed, and without having to examine the causes of these occurrences;

*"(f)* Acts of authority, whether or not they are legally justifiable, and whether or not arbitrary, apart from these for which one party assumes the risk by virtue of other provisions of this contract;

*"(g)* Discontinuance or interruption, for reasons not imputable to the fault of a Party, of normal supplies either of primary products, of materials, of

energy or other items necessary for the performance of the obligations, or significant reduction of such supplies provided that in this latter case, the Party has carried out a reasonable allocation of his supplies between his different co-contracting Parties and provided that in all cases, the Party has shown that he has taken the measures reasonably required of him in these circumstances to provide substitutes;

*"(h)* Default of suppliers or sub-contractors by reason of events affecting them and constituting circumstances releasing from liability, so far as they are concerned, within the meaning of the present contract, provided that the Party has shown that he has taken all measures reasonably required of him to provide substitutes in respect of the defalcation;

*"(i)* Impossibility for the Party to resell the products manufactured—transported—supplied—by virtue of the contract, as a result of any circumstances for which he is not responsible;

*"(j)* Impossibility of securing adequate means of transport by reason of market conditions, any event constituting circumstances releasing from liability within the meaning of the present contract affecting the transport, port, maritime or air installations, or transport by land as well as transport enterprises whose assistance is required for the performance of the contract, provided that the Party has demonstrated that he has taken all measures reasonably required of him to provide substitute in respect of these defalcations;

*"(k)* (Other circumstances may, if desired, be included here in the light of the particular circumstances of the individual contract).

"The parties specify that the following events shall not, in any case, be considered as circumstances releasing from liability:

*"(a)* Refusal of authorisation of licences, of entry and residence permits, or of necessary approvals, to be issued by a public authority of any kind whatsoever so as to permit performance of this contract;

*"(b)* . . . (if desired, insert here other events of which the risk is to be assumed by one of the parties)."

25. The ICC clause is not integrated as part of a set of general conditions applicable to a specific type of contract. It was drafted on the understanding that "it would be necessary to adapt it according to the contract and the requirements of the applicable national law."

### C. Notification

#### 1. Duty to notify

26. The party who relies on an exonerating event is generally required to notify the other party of the event

which prevented the performance of any of his obligations under the contract. The method of notification does not seem to differ much between one type of contract and another, i.e. whether it is one relating to a works contract or a sales contract. The following main types of notification found in contractual stipulations, general conditions, the UNIDO model contracts and the Sales Convention are given below:

By notice in writing

By any means

By notice in writing to be sent by air mail

By cable or telex when such means of communication are available and to be confirmed by registered air mail

By giving notice.

27. In the notification the *force majeure* event may be verified by the following:

By a public authority in the country where the circumstances occurred and operated, e.g. notary public, local or federal government, as the case may be

By consulate

By chamber of commerce

Where *force majeure* occurs outside the supplier's country, the event to be endorsed by local chamber of commerce confirmed by the embassy of the supplier's country residing there.

28. The time within which the notification must be given varies. The following were found:

Immediately

Without delay

Within a time limit agreed.

29. Even in the absence of a specific provision on notification, a party should, nevertheless, inform or advise the other party of an exonerating event in case he may subsequently rely on it.

30. Clause 25.2 of both ECE 188A/574A provides:

"The party wishing to claim relief by reason of any of the said circumstances shall notify the other party in writing without delay on the intervention and on the cessation thereof."

31. The various draft UNIDO model contracts, viz. CRC, TKL and STC require the affected party to give written notice to the other party within ten (10) days of the occurrence of the *force majeure*. The notice must specify the details constituting *force majeure*, with necessary evidence that a contractual obligation is thereby prevented or delayed, and that anticipated period (estimated) during which such prevention, interruption or delay may continue (article 34.2 of each of the models).

32. Under the ICC *force majeure* clause:

"Any Party invoking an event releasing from liability is obliged to inform the other Party of it within a time limit of ( ) days from the moment when it learned of the event and to give a precise description of the event and to communicate all relevant information relating to it, as soon as available so as to permit an appraisal of this event and its effects on performance of the contractual obligations. Termination of the effect of the event releasing from liability will also be communicated within the same time-limit by the Party relying on it."

## 2. Failure to notify

33. In some legal systems, failure to give notification would disentitle the person affected from relying on *force majeure*. However, in other legal systems like many of the common law systems, the doctrine of frustration is not dependent on notice.

34. Where parties expressly make provision for notification in a *force majeure* clause, the consequences to be drawn from failure to give such notification are often spelt out.

35. Under ECE 188A/574A it is expressly stated that the party wishing to claim relief shall notify the other party.

36. Under all the UNIDO models, viz. CRC, TKL and STC reliance on *force majeure* is conditional upon notification being given to the other party (article 34.2 of each of the models).

37. Under article 79(4) of Sales Convention, if notice of the impediment is not given to the other party within a reasonable time, the non-performing party is liable for the damages resulting from such non-receipt, together with other remedies under the Convention which the party may have against him.

38. Under the ICC clause:

"If the Party concerned fails to carry out the communications referred to above, he will automatically lose all right to rely on the event as a circumstance releasing from liability."

## D. Consequences of exoneration

### 1. Effects contemplated by parties in contractual stipulations

39. Depending on variations and precise scope, the following consequences have been incorporated into *force majeure* clauses:

Obligations of defaulting party suspended for duration of event



Delay occasioned by *force majeure* shall automatically lead to an extension of the time for performance—commensurate with such delay

Defaulting party to take reasonable steps to correct the situation as soon as circumstances permit with a view to resuming full performance

Parties will renegotiate the contract

Parties are *entitled to repudiate* the contract after giving notice

*After certain period*, either party may terminate the contract with applicable law as to consequences upon termination.

## 2. ECE 188A and ECE 574A

40. Under ECE 188A/574A if by reason of the circumstances the performance of the contract within a reasonable time becomes impossible, either party shall be entitled to terminate the contract by notice in writing to the other party without requiring the consent of any court (clause 25.3 of both ECE 188A/574A. For details regarding the consequences of termination, see part two, XVII, *Termination*).\*

## 3. FIDIC-CEC

41. The consequences of "special risks" are set out in detail in clause 65:

"Notwithstanding anything in the Contract contained:

"(1) The Contractor shall be under no liability whatsoever whether by way of indemnity or otherwise for or in respect of destruction of or damage to the Works, save to work condemned under the provisions of Clause 39 hereof prior to the occurrence of any special risk hereinafter mentioned, or to property whether of the Employer or third parties, or for or in respect of injury or loss of life which is the consequence of any special risk as hereinafter defined. The Employer shall indemnify and save harmless the Contractor against and from the same and against and from all claims, proceedings, damages, costs, charges and expenses whatsoever arising thereout or in connection therewith.

"(2) If the Works or any materials on or near or in transit to the Site, or any other property of the Contractor used or intended to be used for the purposes of the Works, shall sustain destruction or damage by reason of any of the said special risks the Contractor shall be entitled to payment for:

"(a) Any permanent work and for any materials so destroyed or damaged, and, so far as may be required by the Engineer, or as may be necessary for the

completion of the Works, on the basis of cost plus such profit as the Engineer may certify to be reasonable;

"(b) Replacing or making good any such destruction or damage to the Works;

"(c) Replacing or making good such materials or other property of the Contractor used or intended to be used for the purposes of the Works.

"...

"(4) The Employer shall repay to the Contractor any increased cost of or incidental to the execution of the Works, other than such as may be attributable to the cost of reconstructing work condemned under the provisions of Clause 39 hereof, prior to the occurrence of any special risk, which is howsoever attributable to or consequent on or the result of or in any way whatsoever connected with the said special risks, subject however to the provisions in this Clause hereinafter contained in regard to outbreak of war, but the Contractor shall as soon as any such increase of cost shall come to his knowledge forthwith notify the Engineer thereof in writing.

"...

"(6) If, during the currency of the Contract, there shall be an outbreak of war, whether war is declared or not, in any part of the world which, whether financially or otherwise, materially affects the execution of the Works, the Contractor shall, unless and until the Contract is terminated under the provisions of this Clause, continue to use his best endeavours to complete the execution of the Works. Provided always that the Employer *shall be entitled at any time* after such outbreak of war *to terminate the Contract* . . ."

42. The consequences of "frustration" are described in clause 66:

"If a war, or other circumstances outside the control of both parties, arises after the Contract is made so that either party is prevented from fulfilling his contractual obligations, or under the law governing the Contract, *the parties are released from further performance*, then the sum payable by the Employer to the Contractor in respect of the work executed shall be the same as that which would have been payable under Clause 65 hereof if the Contract had been terminated under the provisions of Clause 65 hereof."

## 4. FIDIC-EMW

43. In clause 47 of FIDIC-EMW the consequences of "special risks" are similar to those in FIDIC-CEC:

"47.1: Notwithstanding anything in the Contract contained, the Contractor shall be under no liability whatsoever whether by way of indemnity or otherwise for or in respect of destruction of or damage to the

\* A/CN.9/WG.V/WP.4/Add.7 (reproduced below).

Works, save to work rejected under the provisions of Clause 28 hereof prior to the occurrence of any special risk hereinafter mentioned, or to property whether of the Employer or third parties, or for or in respect of injury or loss of life which is the consequence of any special risk as hereinafter defined.

"47.2: If the Works or any Plant on or near or in transit to the Site, or any other property of the Contractor used or intended to be used for the purposes of the Works, shall sustain destruction or damage by reason of any of the said special risks the Contractor shall be entitled to payment for:

"(a) Any Portion of the Works or of Plant so destroyed or damaged,

"and so far as may be required by the Engineer, or as may be necessary for the completion of the Works, on the basis of cost plus such profit as the Engineer may certify to be reasonable for

"(b) Replacing or making good any such destruction or damage to the Works;

"(c) Replacing or making good such materials or other property of the Contractor used or intended to be used for the purposes of the Works.

"47.3: Destruction, damage, injury or loss of life caused by explosion or impact whenever and wherever occurring of any mine, bomb, shell, grenade, or other projectile, missile, munition or explosive or war, shall be deemed to be a consequence of the said special risks.

"47.4: The Employer shall repay to the Contractor any increased cost of or incidental to the execution of the Works, other than such as may be attributable to the cost of reconstructing work rejected under the provisions of Clause 28 hereof, prior to the occurrence of any special risk, which is howsoever attributable to or consequent on or the result of or in any way whatsoever connected with the said special risks, subject however to the provisions in these Conditions in regard to outbreak of war, but the Contractor shall as soon as any such increase of cost shall come to his knowledge forthwith notify the Engineer thereof in writing."

44. The following consequences of "frustration" are set out in detail in the FIDIC-EMW Conditions:

*Clause 46:* "If during the currency of the Contract there shall be an outbreak of war (whether war is declared or not) in any part of the world which, whether financially or otherwise, materially affects the execution of the Works the Contractor shall, unless and until the Contract is terminated under the provisions in this Clause contained, use his best endeavours to complete the execution of the Works,

provided always that either the Employer or the contractor shall be entitled, at any time after such outbreak of war, to terminate this Contract . . ." (See also clause 46.2 in part two, XVII, *Termination*.)\*

45. These Conditions also contemplate the possibility of the parties being released from further performance under the law governing the contract:

*Clause 48:* "If a war or other circumstance outside the control of both parties arises after the Contract is made so that under the law governing the Contract the parties are released from further performance then the sum payable by the Employer to the Contractor in respect of the work executed shall be the same as that which would have been payable under Clause 46 if the Contract had been terminated under the provisions of Clause 46."

## 5. UNIDO model contracts (CRC, TKL and STC)

46. The consequences of *force majeure* adopted by the three models are identical in some respects. The non-performing party is excused from "the performance or punctual performance (as the case may be) as from the date of notification of the 'force majeure' for so long as may be justified" (article 34.2 of the respective models). All three models contain a renegotiation clause (see XIV, *Renegotiation, infra*, paragraph 60. For consequences of termination, see part two, XVII, *Termination*).\*

## 6. Sales Convention

47. Paragraph (1) of article 79 provides exemption from liability for a failure to perform obligations due to *force majeure*. Paragraph (5) provides that exemption from liability under the article prevents the other party from exercising only his right to claim damages, but not in respect of other rights under the Convention.

## 7. ICC force majeure clause

48. The consequences of *force majeure* are spelt out in detail with provision for renegotiation:

"The effect of the event releasing from liability is to suspend performance of the obligations which has become impossible as well as of the corresponding obligations (without prejudice to the application of the clauses for adaptation contained in the present contract). No Party will be liable to pay an indemnity on this account. The contractual time limits are extended for a period corresponding to that of the effects of the event releasing from liability.

"During the period of suspension, the parties shall bear permanently half the burden of the costs required for continuation, under the best conditions, of the

\* A/CN.9/WG.V/WP.4/Add.7 (reproduced below).

\* A/CN.9/WG.V/WP.4/Add.7 (reproduced below).

performance of the contractual obligations temporarily suspended.

"Clearance of the said costs shall be carried out either on cessation of the circumstances releasing from liability or on settlement of the accounts in the event of termination of the contract on expiry of the period of suspension."

[Renegotiation provision—see XIV, *Renegotiation*, *infra*, paragraph 64.]

"The parties will retain the fruits of their reciprocal performances carried out previously. They will account to one another. Each party must account to the other for advantages received and kept under the partially performed contract subject to the reservation that the sums due under this provision may not exceed the cost of services tendered, of deliveries carried out, and of goods or other items supplied by the other party. Account will be taken of payments already made by the parties in execution of the terminated contract."

#### XIV. RENEGOTIATION

##### A. General remarks

49. The nature of a works contract necessitates performance over a period of time. Because of a number of factors—for example, economic, fiscal, commercial, legal, political and technological—it is not always possible to proceed with the contract as originally contemplated. Indeed, parties at the outset may not be aware of all factors that may subsequently bear upon the performance of the contract and upon their contractual equilibrium. Even though parties may not be able to carry on with the contract in strict adherence to its terms, it may still be to their mutual advantage not to terminate the contract but to adapt it to the new environment.

50. The mechanism of renegotiation is designed to serve a practical and functional purpose of enabling all parties concerned to review and adapt the contract to changed circumstances when even the more flexible doctrines of *rebus sic stantibus*, *imprévision* and *Wegfall der Geschäftsgrundlage* may not suffice as a conceptual framework for the revision of contracts.

51. Renegotiation of contracts, at least in certain types of contract including a works contract, is a recent phenomenon. But there appears to be a growing awareness that while renegotiation may not provide the panacea to all problems posed by changed circumstances, nevertheless, it enables parties to agree on finding a means of re-establishing their contractual equilibrium. Of course, even in the absence of such a

clause, parties can still review their contract but the insertion of such a clause provides the assurance that parties would resort to some process in order to rescue the contract.

52. There is no renegotiation clause in ECE 188A and ECE 574A, FIDIC-CEC and FIDIC-EMW. In the UNIDO model contracts (CRC, TKL and STC), renegotiation is confined only to *force majeure* situations.

53. The wording of the clauses under study is varied, particularly in the hardship clauses. One reason is that the full implications of changed circumstances, short of rendering the contract incapable of performance under an exoneration clause (see XIII, *Exoneration*, *supra*), have not been fully worked out in most legal systems.

##### B. Renegotiation in event of force majeure

54. In the UNIDO model contracts (CRC, TKL and STC), it was noted that renegotiation was provided for in some *force majeure* clauses (see XIII, *Exoneration*, *supra*, paragraph 46).

##### 1. Contractual stipulations

55. Very few *force majeure* clauses in the Secretariat's collection were found to make provision for renegotiation or adjustment. This is not to say that the renegotiation mechanism is seldom employed.

56. In a works contract between a West European and Middle East entity a renegotiation clause was inserted in a *force majeure* clause to enable parties to "consult with each other" regarding the "future implementation of the agreement." This is an example of a very general clause.

57. Another renegotiation clause found in a recent contract entered into between a West European and African entity reads:

"If 'force majeure' last continuously for ( ) months, then both parties shall without delay meet to consult each other and try to find an appropriate remedy to the situation and to reach agreement thereon. When considering the measure to be taken, the Owner and the Contractor shall give due and serious attention to the difficulties caused by the above-mentioned circumstances, and make serious attempts at finding a fair solution."

58. In contrast to the above clauses, an example may be given of a more specific clause—a time limit is given to the parties to agree to a solution, failure of which entitles either party to cancel the contract. The clause states:

"If any such delay . . . lasts for more than 90 days, the parties shall immediately consult with one another for the purpose of agreeing upon the basis on which

seller resumes production at the end of delay. If they do not agree upon a solution of the problem involved, including adjustment of the price, within 150 days from the beginning of such delay, then either party may, by written notice cancel the portion of the order which is delayed and in such event the Purchaser shall pay to seller reasonable and proper cancellation charges.

59. In some renegotiation clauses express provision is made for the consequences of a breakdown of renegotiation. In others, it is silent. In such a situation the original provisions of the contract will be applicable.

## 2. UNIDO model contracts (CRC, TKL and STC)

60. The wording of the renegotiation provision in the *force majeure* clause in the UNIDO-CRC model differs slightly from that in the UNIDO-TKL. The wording of the latter is identical with that of the UNIDO-STC. The UNIDO-CRC reads:

### "Article 34: Force Majeure

"34.3: The PURCHASER or the CONTRACTOR (as the case may be) shall be diligent in endeavouring to prevent or remove the cause of Force Majeure. Either party upon receipt of the Notice of Force Majeure under Article 34.2 shall confer promptly with the other and agree upon a course of action to remove or alleviate such cause(s), or shall seek alternative methods of achieving the performance objectives under the Contract.

"34.4: If by virtue of Article 34.2, either of the parties is excused from the performance or punctual performance of any obligation for a continuous period of six (6) months then the parties shall consult together to seek agreement as to the required action that should be taken in the circumstances and as to the necessary amendments that should be made to the terms of the Contract.

"34.5: If by virtue of Article 34.2, either of the parties is excused from the performance or punctual performance of any obligation for a continuous period of nine (9) months for one or more causes and if the consultations referred to in the preceding Subarticle 34.4 have not resulted in mutual agreement (or have not taken place because the parties have been unable to communicate with one another), the parties shall thereupon agree to amend the terms of this Contract by virtue of the prevailing Force Majeure circumstances and shall determine the course of further action. If the parties are unable to reach an agreement to amend the terms of this Contract by virtue of the prevailing Force Majeure then the Contract shall be deemed to be terminated pursuant to Article 33 above . . ." (see part two, XVII, *Termination*).\*

61. The UNIDO-CRC counter-proposal seeks to amend the UNIDO-CRC by shortening the period to six months within which the parties must examine the possibility of continuing with the contract in the context of the *force majeure*. Otherwise the parties will have the right to terminate the contract:

### "Article 34: Force Majeure

"34.3: Either party upon receipt of the Notice of Force Majeure under Article 34.2 shall confer as soon as possible with the other and agree upon a course of action to remove or alleviate such cause(s), or shall seek alternative methods of achieving the performance objectives under the Contract, and on the other party upon the relevant consequences on the Contract Price and on the Contract execution time.

"34.4: If the duration of the circumstance of Force Majeure exceeds six (6) months, the Parties shall meet together again to examine the possibility of continuing to carry out the contract. If an agreement cannot be reached upon, the Parties shall have the right to terminate all or part of the contract; in that case the CONTRACTOR shall be indemnified for the consequences of such termination as set forth in Article 33.3."

62. As stated earlier, there is a slight difference in the wording of the UNIDO-CRC model on the one hand and the UNIDO-TKL and UNIDO-STC models on the other. However, the real difference seems to be that while article 33 of the UNIDO-CRC model (dealing with ordinary termination of contract) applies to the termination of a contract in the context of *force majeure* upon failure of an agreement in renegotiation, the counterparts of article 33 in the other models do not apply to the latter models in a similar situation (see part two, XVII, *Termination*).

63. Although the renegotiation provisions in the *force majeure* clauses under study do not expressly state what the position of the contract is during renegotiation, there are other provisions in the *force majeure* clauses which excuse the party affected by *force majeure* from punctual performance or performance.

## 3. ICC force majeure clause

64. The ICC *force majeure* clause makes provision for renegotiation of the contract:

"If the circumstances releasing from liability continues to produce its effects for more than ( ) months, the contract shall be automatically abrogated at the expiry of this period, unless before such expiry the parties, after consulting one another, agree to modify the contract so as to adapt it to the circumstances arising from the occurrence of the event resulting in a release from liability."

\* A/CN.9/WG.V/WP.4/Add.7 (reproduced below).

In the ICC clause, unlike those in the UNIDO model contracts, renegotiation is not mandatory. No provision is made for third party intervention—only the parties to the contract are involved in the readaptation.

### C. Renegotiation in hardship situations

#### 1. Contractual stipulations

65. Renegotiation of contracts to meet fundamental changes particularly in economic or financial events is commonly found in hardship clauses. The scope of such clauses under study varies from a very specific (e.g. limiting the clause to only price-revision) to a general situation.

66. A number of studies on hardship clauses demonstrate that while each type of contract may require certain characteristics not found in other types of hardship clause, the combined totality of the characteristics could well be employed, *mutatis mutandis*, in other types of contract, including, of course, a works contract.

67. In a study of such clauses undertaken by the "International Contracts" study group (under Marcel Fontaine, Director, Centre de Droit des Obligations, Catholic University of Louvain)<sup>1</sup> it was noted that among the types of contract in which hardship clauses were inserted are "large works projects" and "mechanical engineering." It was also noted that "long-term contracts are clearly those where hardship clauses are most frequently stipulated . . ."

68. It should be emphasized that this section of the study is based mainly on the hardship clauses made available to the above-mentioned "International Contracts" study group. Although some of these hardship clauses were taken from "large works projects" and "mechanical engineering" contracts, there was no attempt at isolating them for the purpose of that study.<sup>2</sup> Be that as it may, these hardship clauses examined may well apply to a works contract.

69. An analysis of a number of hardship clauses reveals the following criteria. Some of these criteria are conceived in wider scope while others in narrower scope.

#### (a) Criteria

##### (i) Change in circumstances

This factor has been expressed in the following ways:

(a) "... If at any time during the term hereof either party shall by notice in writing to the other claim upon reasonable grounds . . . that owing to changed circumstances including, but not limited to changes in monetary values or discriminatory Governmental action or regulations . . ."

(b) "In the event of a fundamental change in the conditions which were material to the making of this Agreement, and if from such fact, in order to respect certain provisions, either of the Parties is required to bear unfair hardship, they will meet with a view to modifying the terms and conditions of the present Agreement."

(c) "If either party considers, that owing to changed circumstances, the above price should be revised . . ."

(d) "... if there is the occurrence of an intervening event or change of circumstances . . ."

(e) "... should there be very important changes in circumstances or very significant changes in economic conditions . . ."

Although in some of the above clauses there is the requirement that the change must be "fundamental" and "important" while no such epithets are used in others, nevertheless, it would appear from the consequences that the change of circumstances would have no effect unless it seriously affects the obligations in the contract.

#### (ii) Unforeseeability

The following clauses emphasize the element of unforeseeability:

(a) "... it is impracticable to make provision for every contingency which may arise . . ."

(b) "... circumstances . . . beyond the normal expectations of the parties . . ."

(c) "... in the event of the occurrence of unforeseeable economic developments . . ."

(d) "... extraordinary or unforeseen circumstances . . ."

#### (iii) Event beyond control

The above criterion was contained in the following clauses:

(a) "... an intervening event or change of circumstances beyond said party's control when acting as a reasonable and prudent operator . . ."

(b) "... any circumstances beyond the control of the parties . . ."

The criteria of "unforeseeability" and "event beyond control" of the parties are separate. Failure to appreciate the difference, as seen in some clauses, and a substitute of one for the other would circumscribe the scope of such

<sup>1</sup> See (1976) 2 *Droit et pratique du commerce international*, p. 51.

<sup>2</sup> It is hoped that the Commission would provide the Secretariat with works contracts containing renegotiation provisions. There is a dearth of such documentation at the disposal of the Secretariat. It is also important to examine these clauses in the context of other provisions in the contract itself. In some instances, the Secretariat managed to obtain only specific clauses taken out of their context.

a clause. Other clauses do not mention the two criteria, which of course widens the scope considerably.

(iv) Substantial economic hardship

(a) "... substantial economic hardship ..."

(b) "... which place said party in the situation that ... all annual costs ... associated with or related to (...) which is the subject of this Agreement exceed the annual proceeds derived from the sale of said (...) ..."

(c) "... it, owing to circumstances ..., the economy of the contractual relationships should become modified to the extent of rendering prejudicial, for one of the parties, the discharge of his obligations ..."

(v) Seriousness of events

(a) "... substantial and disproportionate prejudice to either party ..."

(b) "... undue hardship to either party ..."

(c) "... unfairness or substantial and disproportionate prejudice to the interests of either ..."

(b) *Procedure of renegotiation*

70. As noted, hardship clauses invariably provide for renegotiation of the contract. However, problems can arise if the conditions for renegotiation are not precise. A number of clauses under study contain procedures to determine the basis for renegotiation:

(a) "... the (prejudiced) party ... may by notice request the other for a meeting to determine if said occurrence has happened ... If the seller and the buyer have not agreed ... within sixty days ... either party may require the matter to be submitted for arbitration ... The arbitrators shall determine whether the aforesaid occurrence has happened ..."

(b) "In the absence of consensus, it is agreed that each of the parties shall designate an economic expert, assisted if appropriate by a financial expert, and that they shall meet together to determine whether the advantages of the present agreement have been fundamentally disrupted as a result of an unforeseeable event."

71. ICC has also made provision for third party intervention (see *infra*, paragraph 77). Such a procedure may obviate the practical problem which may arise, when the clause is not efficacious due to imprecise drafting and when the party who is not disadvantaged by the "hardship" seeks to prevent the renegotiation.

(c) *Time limit*

72. In some hardship clauses the time between the conclusion of the contract and the point of time when the clause can be invoked is given. For example, the renegotiation clause in the On-Shore (Voltaian Basin)

Petroleum Production Agreement of 1974 between the Government of Ghana and Shell Exploration and Production Company of Ghana Ltd., a subsidiary of Shell International Ltd., reads:

"It is hereby agreed that if during the term of this Agreement there should occur such changes in the financial and economic circumstances relating to the petroleum industry, operating conditions in Ghana and marketing conditions generally as to materially affect the fundamental, economic and financial basis of this Agreement, then the provisions of this Agreement may be reviewed or renegotiated with a view to making such adjustments and modifications as may be reasonable having regard to the operator's capital employed and the risks incurred by him, always provided that *no such adjustments or modifications shall be made within 5 years after the commencement of production area and that shall have no retroactive effect.*"

In a sales contract, a further restriction on the frequency of reliance of the hardship clause was found:

"This section may not be invoked by seller or buyer prior to the first day of October 19... and no more often than once every two years."

(d) *Approach to renegotiation*

73. The hardship clauses under study demonstrate three approaches to renegotiation:

(i) Objective approach

"... in order to restore the parties to a balanced situation comparable to that which obtained at the time that the present contract was concluded."

(ii) Subjective approach

a. "... in fairness to parties ..."

b. "... appropriate and equitable in the circumstances."

c. "... such action as may be appropriate to abate such unfairness or undue hardship ..."

(iii) Hybrid approach

"... with fairness and without substantial and disproportionate prejudice to the interest of the other ..."

(e) *Contract during renegotiation*

74. In the hardship clauses under study, there does not appear to be any express provisions as to the position of the contract during renegotiation. In the context of an

<sup>3</sup> Cited in Asante, "Stability of contractual relations in the transnational investment process" (1979) 28 *International and Comparative Law Quarterly*, pp. 401, 417.

exoneration clause the contract is suspended and may be suspended even if negotiations fail. Whether in events other than exonerating events, the contract will be suspended would depend on express stipulations.

(f) *Decrease or termination of hardship*

75. One such clause which made provision for the situation when the hardship has decreased or terminated reads:

"... To the extent that any occurrence of hardship as determined under this Section 13.9 shall have decreased or ended then any revision of price or other conditions pursuant to an arbitration award shall likewise be changed or ended and the terms and conditions of the Agreement (if not already determined pursuant to paragraph b hereof) shall be restored to take account of the said decrease or ending of the occurrence of hardship."

2. *UNIDO model contracts (CRC, TKL and STC)*

76. Article 33.1 of each of the UNIDO-models appears to deal with a situation which could result in hardship. The article provides that "in the event that the PURCHASER is subject to any circumstances which are wholly unavoidable and/or beyond his control but not including occurrences which are covered by Article 34..."<sup>4</sup> the purchaser is entitled to terminate the contract. It is noted that the clause is couched in very wide language and could cover a situation where no substantial hardship is involved. It may also be noted that no renegotiation is provided unlike in the *force majeure* clause (see *supra*, paragraph 60).

3. *ICC "suggested hardship clause"*

77. The ICC "suggested hardship clause" (Document No. 460/233) is aimed at bringing about renegotiation, on new bases, of a contract which is in the process of being performed when the envisaged change in circumstance occurs. The clause reads:

*"Suggested hardship clause"*

*"(a) Conditions for application"*

"Should there occur after conclusion of the contract circumstances of the following nature: economic, political (including modifications of legislation or administrative measures) or technical, which were unforeseeable for the Parties at the moment the contract was concluded and are outside any control on their part and which destroy the equilibrium of the relations between the Parties making performance of the contract so onerous (though not impossible) for one of them that the burden would exceed all the anticipatory provisions made by the Parties at the time

the agreement was concluded, such Party may request the revision of the present contract.

"This Party must inform the other Party within a time limit of (...) from the moment when it became aware of the event at the same time precisely describing the event relied on and explaining in what way it falls under the provisions of the present article; it will communicate to the other Party without delay every element required for an assessment in the matter in its possession. Unless it carries out this communication, the Party concerned will be automatically excluded from relying on the present article.

"The happening of the event justifying the request for adaptation of the contract does not in any case relieve the Party relying on it from his duty to continue performance of his obligations, nor does it involve a suspension of them.

"(If desired: The Parties agree that the following events in particular fall within the scope of this provision: ...)."

*"(b) Effects"*

"If continuation of the contract by means of a contractual adaptation does not appear economically possible for all the Parties, the Party invoking the benefit of the present clause may terminate the contract without prejudice to the right of the other party to bring any proceedings before the Courts (or: the arbitrator designated in accordance with Article ...) if the conditions for application of the present clause are not fulfilled.

"If continuation of the contract appears economically possible for all the Parties by means of an adaptation, the Parties will immediately consult together with a view to incorporating in the present contract, in good faith and in equity, the adaptations which are necessary, account being taken of the new circumstances and of the risks and burdens that the Parties ought, in any case, to assume. Subject to contrary agreement of the Parties, these negotiations will be carried out during a maximum time limit of (...) months, running from the request to undertake them addressed by one Party to the other.

"The performance of the contract will be continued during these negotiations.

*"Alternative 1"*

"If the negotiations do not succeed within this time limit, the Party invoking the benefit of the present clause may terminate the other contract without prejudice for the right of the other Party to bring any proceedings before the Courts (or: the arbitrator designated in accordance with Article ...) if the conditions for application of the present clause are not fulfilled.

<sup>4</sup> Article 34 deals with *force majeure*. See XIII, *Exoneration*, *supra*, paras. 18 and 60.



*"Alternative 2"*

"If the negotiations do not succeed within this time limit the contract will be readapted by a third Party, designated in accordance with the Rules on Adaptation of Contracts of the International Chamber of Commerce. This third Party will carry out his task on the conditions and in accordance with the procedure provided by the said Rules."

78. In regard to Alternative 2, ICC has drafted Rules for the regulation of contractual relations and related Standard Clauses (1978) which are designed to make third party intervention possible.

79. Although the ICC "suggested hardship clause" is not specifically drafted for use in a specific type of contract, nevertheless, it is designed for general application in international contracts, particularly in contracts involving a series of closely interrelated operations which, in the normal course of events, take place over a number of years.

[A/CN.9/WG.V/WP.4/Add.6\*]

## XV. GUARANTIES

## A. General remarks

1. This study deals with two types of guaranties (a) a guaranty<sup>1</sup> for material, design and workmanship (mechanical guaranty); and (b) a guaranty for the proper performance of the works (performance guaranty).

2. In some contexts "warranty"<sup>2</sup> is used synonymously with "guaranty".

3. There are also various types of "bank" guaranty found in a works contract which are, however, outside the scope of this study.

## B. Mechanical guaranty

4. The mechanical guaranty is called differently in the various forms under study. The ECE General Conditions speak of "guarantee" (clause 23). UNIDO-TKL speaks of "guarantee of workmanship and materials" (article 25) as well as of "warranties" (article 28). UNIDO-CRC uses "mechanical guarantees and warranties" (article 28.3). The FIDIC-EMW Conditions do not use the expression "guaranty" but speak of "defects liability" (clause 33).

5. The function of a mechanical guaranty is generally to limit the extent of the contractor's liability on the one hand and to give assurances and safeguards to the purchaser in regard to quality on the other hand. Clause 33.13 of FIDIC-EMW for instance provides:

"the Contractor shall be under no liability in respect of defects in or damage to the Works or any Section thereof developing or arising after the Works or any Section thereof has been taken over"

save as provided in the Conditions themselves, especially in clause 33.

1. *Extent of guaranty*

6. Under clause 23.1 of both ECE 188A/574A:

"the Contractor undertakes to remedy any defect resulting from faulty design, materials or workmanship."

7. Under clause 33.2 of FIDIC-EMW the contractor is responsible for any defect in or damage to any portion of the works which arises either (a) from any defective materials, workmanship or design, or (b) from any act or omission of the contractor done or omitted during the guaranty period.

8. The UNIDO model contracts, as criticized by an international group of contractors, deal with many questions repetitiously. Thus, for instance, the extent of the mechanical guaranty is covered in articles 25.1, 25.2, 28.1, 28.2, 28.3, 28.4, 28.8 and 28.9 of UNIDO-TKL.

9. Article 28.1 of UNIDO-TKL provides:

"The CONTRACTOR warrants that the Plant, equipment, materials, tools and supplies incorporated in the Works pursuant to this Contract conform with the specifications, plans and all of the contractual criteria, and that the work in every particular is free from defects in design, engineering, processes, materials, workmanship and construction."

10. Article 28.2 of UNIDO-TKL add further elements:

"The CONTRACTOR also warrants as to the correctness and completeness of the plans, all technical data and documents supplied by him as well as to the technical criteria of the equipment fabricated in accordance with his plans and instructions under the present Contract."

11. Article 28.4 of UNIDO-TKL refers to:

"faulty or improper design, workmanship, material, manufacture, fabrication, shipment or delivery."

12. Article 28.8 of UNIDO-TKL includes the warranty of all civil engineering structures,

"and in particular for the foundations for all buildings, plant and equipment."

\* 21 April 1981.

<sup>1</sup> Also spelt as "guarantee".

<sup>2</sup> Also spelt as "warranty".

### 13. Under article 28.9 of UNIDO-TKL:

"The CONTRACTOR warrants that the erection of all Plant and equipment has been accomplished by him in accordance with standard erection codes or as specified in the Annexure . . ."

### 2. Exceptions

14. Contractors do not usually give guaranties without certain exceptions (e.g. normal wear and tear). Furthermore guaranties are given subject to the scrupulous observation and performance by the purchaser of instructions given by the contractor as regards the operation of the plant (e.g. as to the raw materials to be used, a suitable work force and adequate services). In addition, the purchaser is not permitted to carry out any alterations to the plant without the contractor's approval. To sum up, the contractors do not guaranty any defects caused by the purchaser, by third parties or by circumstances beyond their control.

15. Thus clause 23 of both ECE 188A/574A formulates the exceptions from the guaranty as follows:

"23.12: The Contractor's liability does not apply to defects arising out of materials provided, or out of a design stipulated, by the Purchaser.

"23.13: The Contractor's liability shall apply only to defects that appear under the conditions of operation provided for by the Contract and under proper use. It does not cover defects due to causes arising after taking over. In particular it does not cover defects arising from the Purchaser's faulty maintenance or from alterations carried out without the Contractor's consent in writing or from repairs carried out improperly by the Purchaser, nor does it cover normal deterioration."

16. Clause 33.2 of FIDIC-EMW excludes defects which arise from

"a design made, furnished or specified by the Employer and for which the Contractor has disclaimed responsibility in writing within a reasonable time after receipt of the Employer's instructions."

17. According to article 28.7 of UNIDO-TKL:

"the CONTRACTOR's warranty shall not be deemed to cover:

"28.7.1: Damage arising through disregard of the CONTRACTOR's written instructions after Provisional Acceptance by the PURCHASER.

"28.7.2: Normal wear and tear."

18. In their comments to UNIDO-TKL the international group of contractors suggested that "any remaining warranties would be voided" in case the purchaser should "proceed with any remedial measures without the Contractor's approval".

### 3. Period of guaranty

#### (a) Length of period

19. The liability of the contractor is limited to defects which arise during a certain period. In the ECE General Conditions it is called "the Guarantee Period"; in the FIDIC-EMW Conditions "the Defects Liability Period"; and in the UNIDO model contracts "the warranty period".

20. The ECE General Conditions do not specify the guaranty period but leave its determination to the parties. The period may be dependent on the frequency of usage. For example, clause 23.4 of both ECE 188A/574A stipulates that the parties may take into account the intended use of the plant, e.g. one, two or three shifts daily.

Clause 23.4 of ECE 188A provides:

"The daily use of the works and the amount by which the Guarantee Period shall be reduced if the Works are used more intensively are stated in paragraph J of the Appendix."

In contrast, clause 23.4 of ECE 574A provides (a rare instance where it differs from ECE 188A):

"The parties, having taken into account the nature of the Works, may provide in the Contract for a reduction of the Guarantee Period if use of the Works is abnormally intensive."

21. Clause 33.1 of FIDIC-EMW also leaves it to the parties to state the length of the guaranty period in the contract but provides for a period of 12 months if no period is stated. And this clause also takes into account the intensity of the use:

"If the use of the Works by the Employer exceeds that given in the Appendix to the Tender the Defects Liability Period shall be reduced by the amount stated therein."

22. The guaranty period in articles 28.3 and 28.9 of UNIDO-TKL is 12 months.

#### (b) Commencement of period

23. Usually the guaranty period commences on taking-over of the plant (clauses 22.1 and 23.2 of both ECE 188A/574A, clause 33.1 of FIDIC-EMW, and article 28.9 of UNIDO-TKL). Article 28.3 of UNIDO-TKL also refers to the date of provisional acceptance (see part two, X, *Take-over and Acceptance*).

24. If the taking-over is postponed by reason of difficulties encountered by the purchaser, clause 22.3 (d) of both ECE 188A/574A provides:

"the Guarantee Period shall run from the date when the postponed tests have been successfully carried out."

If, however, the purchaser is unwilling to have the taking over tests carried out, the guaranty period "shall start to run on a written notice to that effect being given by the Contractor" (clause 22.2 of both ECE 188A/574A).

(c) *Extension of period*

25. If the plant becomes inoperative because of defects which are covered by the guaranty, the original guaranty period shall be extended to the extent of such non-operation.

26. Thus under clause 23.5 of both ECE 188A/574A, the guaranty period of the works shall be extended:

"by a period equal to the period during which the works are out of action as a result of a defect covered by this Clause."

27. In this regard, clause 33.4 of FIDIC-EMW refers not only to the works but also to portions thereof:

"The Defects Liability Period shall be extended by a period equal to the period during which the Works (or that Portion thereof in which the defect or damage to which the Clause applies has appeared or occurred) cannot be used by reason of that defect or damage . . ."

28. Similarly, article 28.6 of UNIDO-TKL provides:

"... In relation to such other equipment which could not be operated due to the necessity of repair or replacement of the defective part(s) of the Work(s) referred to herein, the warranty period shall be extended by a time equivalent to their periods of non-operation."

(d) *Maximum period of guaranty*

29. Sometimes contracts provide that a maximum period of guaranty is to commence on a date earlier than that of taking-over, e.g. at the first or last delivery of equipment or at the time when a certain percentage of equipment is delivered.

30. Article 28.3 of UNIDO-TKL provides for a maximum period of

"thirty (30) months from the Mechanical Completion of Plant and Equipment under this Contract, if for reasons only attributable to the PURCHASER the plants cannot be started up or brought into commercial production (within the said thirty (30) months period) . . ."

31. In their comments the international group of contractors suggests a reduction of the above period to 18 months and also the substitution of the phrase "reasons only attributable to the Purchaser" by "reasons not attributable to the Contractor."

32. Article 28.3 of UNIDO-CRC provides for a maximum period of 30 months "from the date of shipment".

33. Clause 33.3 and 33.4 of FIDIC-EMW sets a maximum for any extension of the original guaranty period, i.e. two years from the date of taking-over in case of extension where the plant is inoperative by reason of replacements or renewals of parts.

(e) *Special periods for parts*

34. There may well be different guaranty periods in respect of various parts of the plant. Sometimes, special periods are provided for spare parts.

35. Clause 23.3 of both ECE 188A/574A provides:

"In respect of such parts (whether of the Contractor's own manufacture or not) of the Works as are expressly mentioned in the Contract, the Guarantee Period shall be such other period (if any) as is specified in respect of each of such parts."

36. Article 25.10 of UNIDO-TKL contains a special provision in respect of spare parts procured by the contractor on behalf of the purchaser from vendors and/or suppliers. For those parts a special period of guaranty of 12 months "after commencement of use" not exceeding 36 months "after the date of shipment" is provided.

37. For repaired or replaced items the same guaranty period as given originally for the whole plant is usually provided. Thus clause 23.5 of both ECE 188A/574A reads:

"A fresh Guarantee Period equal to that stated in paragraph H of the Appendix shall apply, under the same terms and conditions as those applicable to the original Works, to parts supplied in replacement of the defective parts or to parts renewed in pursuance of this Clause . . ."

38. Similar provisions are contained in clause 33.3 of FIDIC-EMW and article 28.6 of UNIDO-TKL.

#### 4. *Content of guaranty*

(a) *Obligation of contractor*

39. The obligation of the contractor is to remedy (or to make good) the defect (article 23.7 of both ECE 188A/574A, clause 33.2 of FIDIC-EMW, article 28.4 of UNIDO-TKL).

40. The above-mentioned provisions require the contractor to act *forthwith* (ECE and UNIDO) or *with all possible speed* (FIDIC).

41. The same provisions as well as article 25.4 of UNIDO-TKL require the contractor to remedy the defects at his own expense.

42. Clause 23.7 of both ECE 188A/574A deals with the question as to the place *where* the defect is to be cured:

"... Save where the nature of the defect is such that it is appropriate to effect repairs on site, the Purchaser shall return to the Contractor any part in which a defect covered by this Clause has appeared, for repair or replacement by the Contractor, and in such case the delivery to the Purchaser of such part properly repaired or a part in replacement thereof shall be deemed to be a fulfillment by the Contractor of his obligations under this paragraph in respect of such defective part."

43. Clause 33.6 of FIDIC-EMW foresees the possibility of removal of defective work:

"The Contractor may with the consent of the Engineer remove from the Site any Portion of the Works which is defective or damaged if the nature of the defect or damage is such that repairs cannot be expeditiously carried out on the Site."

44. Article 28.5 of UNIDO-TKL lays down the time to be spent in case of replacement:

"... should the removal of the defect require replacement of the equipment, the replacement shall be accomplished in minimal time, plus the shortest possible erection time for this equipment in the CONTRACTOR's country ..."

45. If transport is involved, clause 23.8 of both ECE 188A/574A provides:

"Unless otherwise agreed, the Purchaser shall bear the cost and risk of transport of defective parts and of repaired parts or parts supplied in replacement of such defective parts between the place where the Works are situated and one of the following points:

- (i) The Contractor's works if the Contract is "ex works" or FOR;
- (ii) The port from which the Contractor dispatched the Plant if the Contract is FOB, FAS, CIF, or C and F;
- (iii) In all other cases the frontier of the country from which the Contractor dispatched the Plant."

46. In contrast, article 28.4 of UNIDO-TKL includes transportation cost in the cost to be borne by the contractor.

47. Clause 23.9 of both ECE 188A/574A leaves the apportionment of any additional expenses to the parties or the arbitrator:

"Where in pursuance of paragraph 7 hereof, repairs are required to be effected on site, the incidence of any travelling or living expenses of the Contractor's employees and the cost and risk of transporting any necessary material or equipment shall be settled, in default of agreement between the parties, in such manner as the arbitrator shall determine to be fair and reasonable."

48. Clause 23.10 of both ECE 188A/574A deals with replaced parts:

"Defective parts replaced in accordance with this Clause shall be placed at the disposal of the Contractor."

49. Clause 33.10 of FIDIC-EMW relates to the apportionment of cost in search for the cause of any defect:

"The Contractor shall, if required by the Engineer in writing, search for the cause of any defect, imperfection or fault under the directions of the Engineer. Unless such defect, imperfection or fault shall be one for which the Contractor is liable under the Contract the cost of the work carried out by the Contractor in searching as aforesaid shall be borne by the Employer. But if such defect, imperfection or fault shall be one for which the Contractor is liable as aforesaid the cost of the work carried out in searching as aforesaid shall be borne by the Contractor."

#### (b) Breach of obligation

50. Clause 23.11 of both ECE 188A/574A provides:

"If the Contractor refuses to fulfil his obligations under this Clause or fails to proceed with due diligence after being required so to do, the Purchaser may proceed to do the necessary work at the Contractor's risk and expense, provided that he does so in a reasonable manner."

51. Clause 33.5 of FIDIC-EMW grants the same right to the purchaser "if any such defect or damage be not remedied within a reasonable time".

52. Article 28.4 of UNIDO-TKL deals with the same issue in more detail:

"... If ... the CONTRACTOR shall make default or delay in diligently commencing, continuing and completing the making good of such defect, breakage or failure ... the PURCHASER may proceed to do so independently and to place the work in good operating condition in accordance with the Contract, and the CONTRACTOR shall be liable for all costs, charges and expenses incurred by the PURCHASER in connection therewith and shall forthwith pay the PURCHASER an amount equal to such costs, charges and expenses, upon receipt of invoices certified correct by the PURCHASER."

#### (c) Minor defects

53. Sometimes the purchaser is given the right to rectify minor faults and charge the cost to the contractor. The parties should define in their contract what constitutes a minor fault.

54. Article 28.5 of UNIDO-TKL deals with repair by the purchaser on a case-by-case basis:

"... Subject to prior approval by the CONTRACTOR (which shall not be unreasonably withheld) the PURCHASER shall have the right to repair minor defects at the CONTRACTOR's cost."

#### 5. *Procedure for claims*

55. Clause 23.6 of both ECE 188A/574A provides:

"In order to be able to avail himself of his rights under this Clause the Purchaser shall notify the Contractor in writing without delay of any defects that have appeared shall give him every opportunity of inspecting and remedying them."

56. Clause 33.3 of FIDIC-EMW also requires the purchaser (or the engineer) to inform the contractor forthwith stating in writing the nature of the defect or damage.

57. Article 28.4 of UNIDO-TKL provides for notification in writing from the purchaser whereas article 28.10 of UNIDO-TKL requires immediate information by telegram/telex.

#### 6. *Limitation of or exemption from liability*

58. Often the guaranty of the contractor is limited to the rectification of defects and expressly excludes claims for loss of profit or in respect of personal injury. Thus clause 23.14 of both ECE 188A/574A reads:

"... It is expressly agreed that the Purchaser shall have no claim in respect of personal injury or of damage to property not the subject matter of the Contract arising after taking over nor for loss of profit unless it is shown from the circumstances of the case that the Contractor has been guilty of gross misconduct."

59. According to clause 33.11 of FIDIC-EMW, the contractor is not liable in respect of damage to or loss of property not forming part of the works arising after the expiration of the guaranty period. He is also not responsible for loss of profit "unless it is shown from the circumstances of the case that the Contractor has been guilty of gross misconduct and the circumstances giving rise to the claim occur within the [guaranty] period" as agreed by the parties (if no period is stated, then four years after the date of taking-over). The liability of the contractor is further subject to notice being given by the purchaser within 60 days after the event giving rise to the claim.

60. Clause 23.15 of both ECE 188A/574A and clause 33.12 of FIDIC-EMW contain a nearly identical definition of "gross misconduct". The former reads:

"'Gross misconduct' does not comprise any and every lack of proper care or skill, but means an act or omission on the part of the Contractor implying either a failure to pay due regard to serious consequences

which a conscientious Contractor would normally foresee as likely to ensue, or a deliberate disregard of any consequences of such act or omission."

#### C. *Performance guaranty*

##### 1. *Extent of guaranty*

61. Neither the ECE General Conditions nor the FIDIC Conditions contain any provisions on performance guaranty.

62. The ECE Guide speaks of a guaranty for attainment of the parameters specified in the contract at the time of the acceptance tests (paragraph 41).

63. The UNIDO model contracts contain very detailed provisions on performance guaranty as well as on performance guaranty tests (see part two, X, *Inspection and Tests*).

64. According to article 26.2 of UNIDO-TKL the contractor guaranties that the plant "shall be capable of meeting the full requirements of normal operation, capacity, quality of Products, consumption of raw materials and utilities . . ."

65. The international group of contractors, in commenting on this provision, suggests that the requirements which are guarantied should be precisely stated in the contract.

66. The performance guaranty is given provided that the plant is operated in accordance with the contractor's technical directions and instructions (article 26.2 of UNIDO-TKL).

##### 2. *Demonstration*

67. The performance guaranty is fulfilled if (or when) it has been proven and demonstrated by test runs that the plant meets all the specified requirements.

##### 3. *Content of guaranty*

68. If the performance tests are not successful the performance guaranty is not fulfilled. For the breach of guaranty the parties may agree on various consequences.

69. UNIDO-TKL distinguishes between "absolute" and "penalizable" guaranties. According to article 1.2 absolute guaranties means the performance guaranties of the plants relating to their capacity and quality of the products. Article 1.27 defines penalizable guaranties as the performance guaranties relating to consumption of raw materials and utilities.

70. All the UNIDO models contain very detailed provisions in regard to the various items which fall under the "absolute" or "penalizable" type of performance guaranty. In their comments the international group of contractors observes "that they should not appear in this

amount of detail in model conditions and [that they are] in any event . . . subject to individual negotiation case by case."

71. The contractor is liable to the payment of liquidated damages for non-fulfilment of absolute guaranties at 100% capacity. However, the minimum capacity which is permitted for the purpose of liquidated damages is a 95% capacity. Where the capacity falls short of a 95% capacity other remedies are available (article 27.1.4 of UNIDO-TKL).

72. For the non-fulfilment of penaltiable guaranties, the contractor is liable to the payment of specified amounts of money if he does not rectify the defects (article 27.2 of UNIDO-TKL).

## XVI. RECTIFICATION OF DEFECTS

### A. *Meaning of "defect" in works contract*

73. "Defect" in a works contract covers any condition which adversely affects the quality of the work. The defect may be due to faulty design, defective workmanship or materials. The plant and material will be regarded as defective if it is not in accordance with the description of the work to be found in the contract as a whole. Strict adherence to the contract terms is particularly important in a works contract. Indeed, one of the basic obligations of the contractor is to deliver the works free of defects; even in the absence of an express provision to this effect, this obligation will be implied.

74. Defects may appear at any one of the following stages: during production, at taking-over, during the guaranty period and after the expiration of the guaranty period.

### B. *Defects during production*

#### 1. *Removal of defects*

75. Once a defect has been discovered a purchaser has an interest in ensuring that it is cured as early as possible. The purchaser should not have to wait until completion of the work before intervening. Most of the forms under study therefore empower the engineer to issue instructions when defects appear at any time during production. Clause 39.(1) of FIDIC-CEC provides:

"The Engineer shall during the progress of the Works have power to order in writing from time to time

"(a) The removal from the Site, within such time or times as may be specified in the order, of any

materials which, in the opinion of the Engineer, are not in accordance with the Contract

"(b) The substitution of proper and suitable materials and

"(c) The removal and proper re-execution, notwithstanding any previous test thereof or interim payment therefor, of any work which in respect of materials or workmanship is not, in the opinion of the Engineer, in accordance with the Contract."

76. The above provision emphasizes the duty of the contractor to comply strictly with the requirement of the contract. Previous approval of or payment for the materials by the purchaser will not relieve the contractor of this responsibility.

77. The FIDIC-EMW Conditions also give the engineer the right to intervene during production, and to order the re-execution of the works. Clause 28 provides:

"If, in respect of any Section or Portion of the Works not yet taken over, the Engineer shall at any time:

"(a) Decide that any work done or Plant supplied or materials used by the Contractor or any Sub-Contractor is or are defective or not in accordance with the Contract, or that such Section or Portion of the Works is defective or does not fulfil the requirements of the Contract . . . and

"(b) As soon as reasonably practicable give to the Contractor notice in writing of the said decision specifying particulars of the defects alleged and of where the same are alleged to exist or to have occurred, and

"(c) So far as may be necessary place the Plant at the Contractor's disposal,

"then the Contractor shall with all speed . . . at his own expense, make good the defects so specified."

78. Under the UNIDO model contracts, the activities in relation to the rectification and modification of the plant prior to provisional acceptance are the responsibility of the contractor to be performed at his own cost within a stipulated time. Article 29.6 of UNIDO-CRC provides:

"Should the CONTRACTOR discover any discrepancy or mistake in his process, engineering, instructions, specifications, inspections or procurement, or errors or omissions as the case may be which require rectification(s) to be undertaken to correct the defects . . . the CONTRACTOR and the PURCHASER shall meet and agree to such extension in time to be allowed the CONTRACTOR for the rectification of defects and corrective engineering."

79. Under the UNIDO-TKL and UNIDO-STC model contracts, the contractor is given the power to modify or

re-execute the work at his own discretion. UNIDO-TKL states:

"Article 29.12: The CONTRACTOR's obligations to execute the modifications, corrections, rectifications and replacement of equipment . . . shall not be restricted."

80. The ECE 188A/574A General Conditions give the purchaser a right to inspect the materials before they are delivered to the construction site (for further details regarding the parties' obligations, see part two, VIII, *Inspection and Tests*).<sup>\*</sup> If defects are detected during the inspection the ECE General Conditions do not expressly state the contractor's obligation to remedy the defects: clause 8.2 of both ECE 188A/574A states:

"If as a result of such inspection and checking the Purchaser shall be of the opinion that any materials or parts are defective or not in accordance with the Contract, he shall state in writing his objections and the reason therefor."

81. It would, however, be in the interest of the contractor to remedy the defects which have been detected.

## 2. Suspension of the work

82. To avoid delay and additional costs it is always in the interests of the contractor and purchaser to carry out an investigation as soon as symptoms of a defect appear. A suspension of the works may be necessary in order to discover the cause of the defect and to prevent further damage to the works.

83. The FIDIC-CEC and FIDIC-EMW Conditions define the situation in which the contractor shall suspend the work either at his own expense or at the expense of the purchaser. Clause 40.(1) of FIDIC-CEC states:

"The Contractor shall, on the written order of the Engineer, suspend the progress of the Works or any part thereof . . . The extra cost incurred by the Contractor in giving effect to the Engineer's instructions under this Clause shall be borne and paid by the Employer unless such suspension is

"(a) Otherwise provided for in the Contract, or

"(b) Necessary by reason of some default on the part of the Contractor . . ."

84. The UNIDO model contracts also have provisions requiring the contractor to suspend the work during construction, at the instruction of the purchaser. Article 32.1 of UNIDO-CRC states:

"The PURCHASER may, when in the PURCHASER's opinion it is deemed necessary, require the CONTRACTOR to suspend execution of the work or part of the work, either for a specified or unspecified

period by communicating notice to that effect to the CONTRACTOR . . ."

85. The ECE General Conditions do not contain express provisions requiring the suspension of the works.

## C. Defects at taking-over

86. All the forms under study contain provisions for inspection and tests upon completion to ensure that the plant meets the contract requirements (for further details, see part two, VIII, *Inspection and Tests*). Under most of these forms the issuance of a completion certificate is conditional upon the removal of defects which are discovered during the inspection. Clause 48.(1) of FIDIC-CEC states:

" . . . The Engineer shall, within twenty-one days of the date of delivery of such notice . . . give instructions in writing to the Contractor specifying all the work which, in the Engineer's opinion, requires to be done by the Contractor before the issue of such Certificate. The Engineer shall also notify the Contractor of any defects in the Works affecting substantial completion that may appear after such instructions and before completion of the works specified therein. The Contractor shall be entitled to receive such Certificate of Completion within twenty-one days of completion to the satisfaction of the Engineer of the works so specified and making good any defects so notified."

87. Under the FIDIC-EMW there is also a provision requiring that the plant shall pass the completion tests before a taking-over certificate can be issued. Should the plant fail to pass the tests or repetition thereof, then, according to clause 29.6,

" . . . the Engineer shall be entitled:

" . . .

"(b) To reject the Works or Section thereof in accordance with Clause 28 (Defects before taking-over)<sup>3</sup> if the results of the tests show that the Works or the Section fail to meet the performance guarantees or the agreed tolerances specified in the Contract, or if there are no such guarantees or tolerances, the results show that the Works or the Section are not in accordance with the Contract . . ."

88. Under the UNIDO model contracts, the contractor has, upon completion, the obligation to demonstrate that the plant meets the performance guarantees contained in the contract.

89. According to the UNIDO-CRC model, if the plant fails the performance tests the obligation of the contractor to rectify the plant at his own cost would depend upon whether or not the defect is due to the

<sup>\*</sup> A/CN.9/WG.V/WP.4/Add.3 (reproduced above).

<sup>3</sup> See paragraph 77, *supra*.



contractor's own fault or to matters falling within his responsibility. Article 29.1 states:

"In the event that due to mistakes, negligence or errors in the processes and/or in the detailed engineering performed by the CONTRACTOR and/or in the CONTRACTOR's procurement, or specifications, instructions and inspections, or for whatever reason falling within the CONTRACTOR's obligations, the CONTRACTOR is unable to demonstrate the Absolute Guarantees . . . the CONTRACTOR shall proceed to effect the rectifications, modifications, additions and/or changes which in the CONTRACTOR's professional judgment are necessary to eliminate the defects and/or faults and thereby to achieve the specified guarantees . . ."

90. Under the UNIDO-CRC model the plant will not be taken-over until the plant's capability to meet performance guaranties has been demonstrated. Article 29.7 provides:

"The CONTRACTOR's obligation to rectify defects and to take corrective steps shall continue unabated even if the period of extension . . . is exhausted, and the CONTRACTOR shall continue his endeavours at his own cost to rectify the defects and take corrective measures . . . The obligation of the CONTRACTOR herein shall not end until the Absolute Guarantees of the Plants are successfully demonstrated."

91. The UNIDO-TKL model has similar provisions requiring the contractor to demonstrate the plant's capability to meet performance guaranties and to perform the intended function.

92. Under the UNIDO-TKL and UNIDO-STC models, the contractor, before proceeding to execute the work, shall consult with the purchaser on the nature of the defect. The extent of the contractor's responsibility will depend upon the seriousness of the defect. Article 29.8 of UNIDO-TKL provides:

"Whenever any of the defects . . . appear, the CONTRACTOR shall immediately thereafter advise the PURCHASER, and the procedure specified hereunder shall apply in connection with any repair and/or replacement . . . The defective material, machinery and/or equipment shall be examined by the CONTRACTOR and PURCHASER (or their duly authorized representatives).

"29.8.1: In the event that the defect and/or damage is agreed to be minor the CONTRACTOR shall satisfactorily rectify the same through the most expeditious means.

"29.8.2: In the case of a serious or extensive defect or damage the CONTRACTOR shall state the method of making good the defect or damage in any event at his own cost, and one of the following methods shall be adopted, subject however to the considerations of efficiency, speed and the contractual time schedules:

"29.8.2.1: The undertaking of repair/rectification work or alteration at Site.

"29.8.2.2: Removal of the defective material or equipment from the Site and the undertaking of repair or rectification away from the Site.

"29.8.2.3: The removal of defective material, machinery or equipment and replacement by new and unused materials, machines or equipment."

93. Under the ECE General Conditions there are also provisions for taking-over tests to ensure that the plant is in conformity with the contract requirements. If defects are detected during the tests, clause 21.2 of both ECE 188A/574A states:

"If as a result of such tests the Works are found to be defective or not in accordance with the Contract, the Contractor shall with all speed and at his own expense make good the defect or ensure that the Works comply with the Contract . . ."

94. Where the taking-over tests are delayed by the purchaser and defects appear in the interim, the purchaser must bear the cost of rectifying such defects. Article 22.3 of both ECE 188A/574A provides:

"If by reason of difficulties encountered by the Purchaser . . . it becomes impossible to proceed to the taking-over tests . . .

". . .

"(c) The Contractor may, at the cost of the Purchaser . . . make good any defect or deterioration therein that may have developed, or loss thereof that may have occurred, after the date when the Works were first ready for testing in accordance with the Contract."

95. Under the FIDIC-CEC, defective work at taking-over covers: work outstanding at the date of completion, work which does not comply with the contract requirements and which under the contract is explicitly or impliedly within the responsibility of the contractor. Under FIDIC-CEC the contractor is obliged to rectify these defects at his own cost; defects due to any other cause shall also be rectified by the contractor but at the expense of the purchaser. Clause 49 states:

"(2) To the intent that the Works shall at or as soon as practicable after the expiration of the Period of Maintenance be delivered to the Employer in the condition required by the Contract, fair wear and tear excepted, to the satisfaction of the Engineer, the Contractor shall finish the work, if any, outstanding at the date of completion . . . as soon as practicable after such date and shall execute all such work of repair, amendment, reconstruction, rectification and making good defects, imperfections, shrinkages or other faults as may be required of the Contractor in writing by the Engineer during the Period of Maintenance, or within fourteen days after its expiration, as a result of an

inspection made by or on behalf of the Engineer prior to its expiration.

"(3) All such work shall be carried out by the Contractor at his own expense if the necessity thereof shall, in the opinion of the Engineer, be due to the use of materials or workmanship not in accordance with the Contract, or to neglect or failure on the part of the Contractor to comply with any obligation, expressed or implied, on the Contractor's part under the Contract."

#### D. Defects during the guaranty period

96. Most of the forms examined expressly require the contractor to rectify defects which appear during the guaranty period.

97. A dispute can arise whether a defect is due to a matter within the contractor's obligation. Under the FIDIC-CEC Conditions, the engineer determines whether the contractor is liable in this situation. Clause 49.(3) provides:

"... If, in the opinion of the Engineer, such necessity shall be due to any other cause, the value of such work shall be ascertained and paid for as if it were additional work."

98. Under the FIDIC-EMW Conditions, the contractor's obligation to re-execute the work will depend upon whether the defects are due to matters within his responsibility. Clause 33.2 states:

"The Contractor shall be responsible for making good with all possible speed at his expense any defect in or damage to any portion of the Works which may appear or occur during the Defects Liability Period and which arises either:

"(a) From any defective materials, workmanship or design ... or

"(b) From any act or omission of the Contractor done or omitted during the said period."

99. The UNIDO model contracts state a period within which the contractor shall cure the defects. Under the UNIDO-TKL and UNIDO-STC, the purchaser has the authority to specify the time within which the contractor has to re-execute the work. Article 29.10 of UNIDO-TKL provides:

"... The PURCHASER ... shall provide the CONTRACTOR with an allotted time upon specified conditions ... for the undertaking of such modifications, rectification(s), replacement(s), corrective engineering ... and (if applicable) the making good of faulty workmanship and defective materials ..."

100. The specified time may be extended at the purchaser's discretion. Article 29.10 of UNIDO-TKL states:

"... The CONTRACTOR shall complete the work in conformity with the requirements of the Contract and shall (at the discretion of the PURCHASER) be granted such further extensions as may be necessary without prejudice to any of the PURCHASER's rights ..."

101. Under the UNIDO-CRC the time within which the contractor shall rectify the defects is stated in advance, subject to a right to have the time extended under specified conditions. Article 29.8 of UNIDO-CRC provides:

"The CONTRACTOR's obligations to execute the rectifications ... shall be limited to twelve (12) months from the date of start-up of the Plant(s), however the period during which the Plant(s) cannot be operated normally due to any default on the part of the PURCHASER or the period in excess of ten (10) months spent in the replacement of equipment (if any such replacement is required from Vendors) shall not be counted in computing the said twelve (12) months period."

102. The ECE General Conditions require the contractor to rectify defects during the guaranty period forthwith and at his own expense (clause 23.7 of both ECE 188A/574A). (For a discussion of the parties' obligations during the guaranty period, see XV, *Guaranties, supra*.)

#### E. Requirement of notice

##### 1. Obligation to notify and form of notice

103. After taking-over only the purchaser has the practical means of detecting defects. Most of the forms analysed therefore require the purchaser to give notice of defects which appear after taking-over.

104. Most of the forms under study state that the contractor should be given written notice of a defect. The form and content of the notice will depend upon the nature of the defect and upon whether the defect is discovered before or after taking-over. If the defect occurs before taking-over and is due to the contractor's default, a general notice will normally suffice.

105. The FIDIC-CEC Conditions state only that the notice of defect during production and maintenance periods should be given in writing (see paragraph 75, *supra*).

106. Under clause 28 of FIDIC-EMW Conditions (see paragraph 77, *supra*) written notice has to contain particulars of the defect stating the extent of the work to be done.

107. Under the UNIDO model contracts, the contractor is obliged to give the purchaser notice of any defects which may appear before taking-over. The form

and content of the notice is not stated. Article 29.5 of UNIDO-STC provides:

"Should any defects . . . occur, the CONTRACTOR shall immediately thereafter advise the PURCHASER, and the procedure specified hereunder shall apply in connection with any rectification and/or modification work . . ."

## 2. Failure to notify

108. Under the forms analysed, the purchaser's failure to give notice of defects which appear during production does not absolve the contractor from his liability for defective work. Most of the forms under study, however, do not state the consequences of the purchaser's failure to give notice of defects which may appear after taking-over.

109. Under the ECE General Conditions, written notice of defects is a precondition to the purchaser's exercise of his rights under the guaranty provisions. Clause 23.6 of both ECE 188A/574A states:

"In order to be able to avail himself of his rights under this Clause the Purchaser shall notify the Contractor in writing without delay of any defects that have appeared and shall give him every opportunity of inspecting and remedying them."

## F. Failure to remedy defects

110. The FIDIC-CEC and FIDIC-EMW Conditions contain express provisions entitling the purchaser to bring another contractor on the site to do the required work on the failure of the original contractor to re-execute the work. In certain defined circumstances the purchaser has a right of forfeiture and termination of the contract.

111. On the contractor's failure to do the required work during construction, clause 39.(2) of FIDIC-CEC provides:

"In case of default on the part of the Contractor in carrying out such order, the Employer shall be entitled to employ and pay other persons to carry out the same and all expenses consequent thereon or incidental thereto shall be recoverable from the Contractor by the Employer, or may be deducted by the Employer from any monies due or which may become due to the Contractor."

112. There is a similar provision under the FIDIC-CEC Conditions. In the event of failure by the contractor to remedy defects which appear during the "maintenance" period, clause 49.(4) of FIDIC-CEC states:

"If the Contractor shall fail to do any such work . . . the Employer shall be entitled to employ and pay other persons to carry out the same and if such work is

work which, in the opinion of the Engineer, the Contractor was liable to do at his own expense under the Contract, then all expenses consequent thereon or incidental thereto shall be recoverable from the Contractor by the Employer . . ."

113. The FIDIC-EMW Conditions require the contractor to act expeditiously in remedying the defects; if he does not do so the purchaser may do the required work at the cost of the contractor. Clause 28 provides:

". . . In case the Contractor shall fail so to do the Employer may, provided he does so without undue delay, take at the cost of the Contractor such steps as may in all the circumstances be reasonable to make good such defects . . ."

114. Under the UNIDO model contracts the purchaser is entitled to take any measures to carry out the remedial work. Article 29.3 of UNIDO-CRC provides:

"If the CONTRACTOR shall neglect or refuse to take the necessary measures to ensure the elimination of the defects and/or faults within a reasonable time, then the PURCHASER may take such remedial steps to carry out the engineering, procurement, inspection and supervision of erection of new equipment or undertake repair and/or replacement of used equipment to rectify the defects and correct all associated problems, and the cost of such remedial steps taken by the PURCHASER shall be to the CONTRACTOR's account, and/or may be recovered in any manner at the discretion of the PURCHASER."

115. Under the UNIDO-CRC, where a contractor fails to perform the required work within the stipulated time, and the purchaser does not consent to the extension of time, the purchaser is given the right to terminate the contract. Article 29.4 provides:

"In the event that . . . the PURCHASER does not agree to further extend any periods requested by the CONTRACTOR for such modifications, additions, and/or changes, the PURCHASER shall have the right to terminate the Contract . . ."

116. The UNIDO-TKL and UNIDO-STC model contracts make reference to the purchaser's right of recourse to his other remedies under the contract if the defects are not cured within the stipulated time. Article 29.13 of UNIDO-TKL states:

"Any extension of time granted to the CONTRACTOR shall be without prejudice to any rights or remedies of the PURCHASER whatsoever under this Contract, should the CONTRACTOR fail to accomplish work within the extended time so allowed."

117. The ECE General Conditions limit the contractor's liability to the obligations defined under the guaranty (for further details, see XV, *Guaranties, supra*).

### G. Defects after the guaranty period

118. The liability for defects ceases at the expiration of the guaranty period. The contractor has no contractual obligation to rectify defects which appear outside this period. As a matter of good practice, contractors would, at the purchaser's request, repair any defects which may appear outside the guaranty period at the expense of the purchaser.

[A/CN.9/WG.V/WP.4/Add.7\*]

## XVII. TERMINATION

### A. General remarks

1. In this study the term "termination" denotes the dissolution of a contract brought about by breaches of obligation, exonerating circumstances or other grounds. It may be noted that a contract can be put to an end only for the future or retrospectively. The term "termination" in this study also covers "rescission", "cancellation" and "avoidance" of a contract.

2. In a works contract a termination clause usually makes provision for only serious breaches of obligation (see part two, VII, *Quality*\*\* and XI, *Delays and Remedies*\*\*\* or for non-performance due to exonerating circumstances (see part two, XIII, *Exoneration*).\*\*\*\*

### B. Grounds for termination

#### 1. Breach of contract

3. To put an end to a works contract is never a decision to be taken lightly nor is it one of slight consequence. The costs involved in a particular works contract coupled with the nature of its performance may render the question of termination one in which the parties would only have recourse to after all other remedies prove ineffective.

##### (a) Breach of contract by the contractor

4. Not every breach of contract is serious enough to enable the aggrieved party to terminate the contract. The Sales Convention recognizes this fact and grants the buyer and the seller the right to avoid the contract only in specific cases. Article 49 of the Sales Convention provides:

"(1) The buyer may declare the contract avoided:

"(a) If the failure by the seller to perform any of his obligations under the contract or this Convention amounts to a fundamental breach of contract; or

"(b) In case of non-delivery, if the seller does not deliver the goods within the additional period of time fixed by the buyer in accordance with paragraph (1) of article 47 or declares that he will not deliver within the period so fixed."

5. Article 25 of the Sales Convention contains a definition of what is to be considered as a fundamental breach: one which results in such detriment to the other party as substantially to deprive him of what he is entitled to expect under the contract, unless the party in breach did not foresee and a reasonable person of the same kind in the same circumstances would not have foreseen such a result.

6. In a works contract the parties usually specify in detail the grounds for termination.

##### (i) Delay in completion

7. It is not uncommon to find certain delays in the completion of a large industrial plant. Before the purchaser is given the right to terminate the contract he must usually give the contractor an additional period of time to complete the works. For instance clause 20.5 of both ECE 188A/574A provides:

"If any portion of the Works . . . remains uncompleted, the Purchaser may by notice in writing to the Contractor require him to complete and . . . fix a final time for completion . . . If . . . the Contractor fails to complete within such time, the Purchaser shall be entitled . . . to terminate the Contract in respect of such portion of the Works."

8. A similar provision is contained in clause 31.2 of FIDIC-EMW. The relevant portion of the clause reads:

"If for any reason, other than one for which the Employer or some other contractor employed by him is responsible, the Contractor fails to complete within such time, the Employer may by further written notice to the Contractor elect

"either (a) To require the Contractor to complete,

"or (b) To terminate the Contract in respect of such Portion of the Works . . ."

In contrast to the position in some other forms under study, the above clause does not require the employer to terminate the contract even after failure of the contractor to complete within the additional period of time which had been given to him. The purchaser is still given the option to require the contractor to complete the works.

9. The UNIDO model contracts also treat the question of delay as a ground for termination of the

\* 3 April 1981.

\*\* A/CN.9/WG.V/WP.4/Add.2 (reproduced above).

\*\*\* A/CN.9/WG.V/WP.4/Add.4 (reproduced above).

\*\*\*\* A/CN.9/WG.V/WP.4/Add.5 (reproduced above).

Contract. For example article 33.7.1 of UNIDO-TKL provides:

"Where the CONTRACTOR has made default or delayed in commencing or in executing, completing or delivering the work or any portion thereof to the reasonable satisfaction of the PURCHASER, and the PURCHASER has given notice thereof to the CONTRACTOR and has by such notice required the CONTRACTOR to put an end to such default or delay, and such default or delay continues for a period of ( . . . ) after such notice was given; . . . the PURCHASER may, without any other authorization, cancel the Contract . . .

10. Article 33.7.4 of UNIDO-TKL further provides that the purchaser has the right to cancel the contract when the contractor has "abandoned" the work.

11. Before dealing with the FIDIC Conditions further it must be noted that they give the purchaser the right to terminate not in all cases of breach of contract by the contractor. According to these Conditions in some situations the purchaser has the right to "enter upon the Site and expel the Contractor therefrom *without thereby voiding* the Contract, or releasing the Contractor from any of his obligations or liabilities under the Contract, or affecting the rights and powers conferred by the Contract on the Employer or the Engineer . . ." (Clause 44.1 of FIDIC-EMW) This right is dealt with here under termination since its effects are quite similar to those of an ordinary termination clause. It would appear that this approach is to give as much protection as possible to the purchaser.<sup>1</sup>

12. Clause 44.1 of FIDIC-EMW provides, *inter alia*, the following contingencies as grounds for expelling the contractor:

" . . . if the Engineer shall certify in writing to the Employer that in his opinion the Contractor:

"(a) Has abandoned the Contract, or

"(b) Without reasonable excuse has failed to commence the Works or has suspended the progress of the Works for twenty eight days after receiving from the Engineer written notice to proceed . . ."

13. Clause 63.(1) of FIDIC-CEC is identical to the above clause but goes further by adding that if the contractor:

"(c) Has failed to remove materials from the Site or to pull down and replace work for twenty-eight days

after receiving from the Engineer written notice that the said materials or work had been condemned and rejected by the Engineer under these conditions . . ."

(ii) Non-conformity of work

14. Not only does the delay in completion cause serious difficulties to the purchaser but also breach of contractual stipulations regarding quality (see part two, VII, *Quality*). Clause 44.1 of FIDIC-EMW, therefore, provides that the purchaser may expel the contractor with the legal effect as described in paragraph 11 *supra*,

" . . . if the Engineer shall certify in writing to the Employer that in his opinion the Contractor:

" . . .

"(c) Despite previous warnings by the Engineer, in writing, is not executing the Works in accordance with the Contract, or is neglecting to carry out his obligations under the Contract so as seriously to affect the carrying out of the Works . . ."

15. Clause 63.(1) of FIDIC-CEC is worded slightly differently although the effect is similar. Here the purchaser has the right to expel the contractor, if the contractor,

"(d) Despite previous warnings by the Engineer, in writing, is not executing the Works in accordance with the Contract, or is persistently or flagrantly neglecting to carry out his obligations under the Contract . . ."

(iii) Unauthorized assignment and sub-contracting

16. The construction of large industrial works requires skill and experience by the contractor. The assignment of a works contract to a third party is therefore usually possible only with the consent of the purchaser.

17. Some conditions treat unauthorized assignment by the contractor as serious enough to give the purchaser the right to terminate the contract. According to clause 44.1 of FIDIC-EMW and clause 63.(1) of FIDIC-CEC the employer may enter upon the site and expel the contractor therefrom "[i]f the Contractor shall assign the Contract, without the consent in writing of the Employer first obtained . . ."

18. Article 33.7 of UNIDO-TKL grants the purchaser the right to cancel the contract "where the CONTRACTOR has . . . made an assignment of the Contract without the approval of the PURCHASER."

19. On the other hand, sub-contracting is very common in the construction of large industrial works. Unless it is not prohibited by the contract sub-contracting *per se* does not give rise to objections. The contractor must make sure, however, that any sub-contracting does not affect the proper execution of the work. Clause 63.(1) of FIDIC-CEC gives the purchaser the right to expel the contractor "if the Engineer shall certify in writing to the Employer that in his opinion the

<sup>1</sup> On the other hand, in case of breach of contract by the purchaser the contractor has the right to terminate the contract under the FIDIC Conditions. (Clause 41.3 of FIDIC-EMW speaks of "to terminate the Contract" while clause 51.1 of FIDIC-EMW, "to terminate his employment under the Contract.") It may also be noted that in case of bankruptcy of the contractor the purchaser may terminate the contract under clause 45 of FIDIC-EMW while under clause 63.(1) of FIDIC-CEC, he may only expel the contractor. These are further discussed below. The reasons for such distinction in treatment are not clear.

Contractor: . . . (e) has, to the detriment of good workmanship, or in defiance of the Engineer's instructions to the contrary, sub-let any part of the Contract . . ."

(b) *Breach of contract by the purchaser*

20. Under article 64 of the Sales Convention:

"(1) The seller may declare the contract avoided:

"(a) If the failure by the buyer to perform any of his obligations under the contract or this Convention amounts to a fundamental breach of contract; or

"(b) If the buyer does not, within the additional period of time fixed by the seller in accordance with paragraph (1) of article 63, perform his obligation to pay the price or to take delivery of the goods, or if he declares that he will not do so within the period so fixed."

21. Similar grounds for termination are found in works contracts.

(i) *Non-taking of delivery*

22. The failure to take delivery of the plant by the purchaser on the due date constitutes a breach of contract (see part two, X, *Acceptance and Take-over*).\* In such a case, according to clause 10.2 of both ECE 188A/574A "the Contractor may require the Purchaser by notice in writing to accept delivery within a reasonable time. If the Purchaser fails for any reason whatever to do so within such time, the Contractor shall be entitled . . . to terminate the Contract in respect of such portion of the Plant as is by reason of the failure of the Purchaser aforesaid not delivered . . ."

23. The FIDIC Conditions grant the contractor the right to terminate the contract "in the case of the Engineer's failure to issue an interim certificate . . ." (clause 41.3 of FIDIC-EMW), or "in the event of the Employer: . . . (b) interfering with or obstructing the issue of any certificate of the Engineer . . ." (clause 51.1 of FIDIC-EMW).

24. For the last-mentioned case, above, FIDIC-CEC clause 69.(1) uses the wording: "(b) interfering with or obstructing or refusing any required approval to the issue of any such certificate . . ."

25. The UNIDO model contracts do not contain similar provisions.

(ii) *Non-payment*

26. Clause 11.7 of both ECE 188A/574A gives the contractor the right to terminate the contract if the purchaser has not made payment within a period of delay stipulated by the parties.

27. Under the FIDIC Conditions the contractor is entitled "to terminate his employment under the Con-

tract" according to clause 69.(1) of FIDIC-CEC (see also clause 51.1 of FIDIC-EMW):

"In the event of the Employer:

"(a) Failing to pay to the Contractor the amount due under any certificate of the Engineer within thirty days after the same shall have become due under the terms of the Contract . . ."

2. *Exonerating circumstances*

28. Apart from termination on the ground of breach, exonerating circumstances constitute one of the most common grounds for the termination of a works contract. Two cases may be distinguished: first, where certain circumstances make any further performance impossible and secondly, where circumstances prevent performance for a period of time (see part two, XIII, *Exoneration*).\*

29. Under clause 25.3 of both ECE 188A/574A, if circumstances beyond the control of the parties affect the timely performance of the obligations by the parties, and "if, by reason of any of the said circumstances, the performance of the Contract within a reasonable time becomes impossible, either party shall be entitled to terminate the Contract . . ."

30. The FIDIC Conditions also provide for the termination of the contract when one of the parties is prevented from performing because of the outbreak of war. (Clause 46.1 of FIDIC-EMW; clause 65.(6) of FIDIC-CEC).

31. Apart from war as above-mentioned, the FIDIC Conditions do not make provision for termination in other exonerating circumstances.

32. Under the UNIDO model contracts, the purchaser is allowed to terminate the contract in the event that the purchaser is subject to any circumstances which are wholly unavoidable and/or beyond his control (article 33.1 of UNIDO-TKL).

33. In the case of a prevailing and continuous *force majeure* the UNIDO model contracts make provision for the possibility of termination of the contract by both parties (article 34.5 of UNIDO-TKL).

3. *Other grounds for termination*

34. In some forms under study other grounds are also included for termination. They relate to the financial situation of the other party.

35. The FIDIC Conditions deal with the case of bankruptcy of the contractor and of the purchaser separately. Clause 63.(1) of FIDIC-CEC provides that the purchaser may expel the contractor

\* A/CN.9/WG.V/WP.4/Add.3 (reproduced above)

\* A/CN.9/WG.V/WP.4/Add.5 (reproduced above).

"[i]f the Contractor shall become bankrupt, or have a receiving order made against him, or shall present his petition in bankruptcy, or shall make an arrangement with or assignment in favour of his creditors, or shall agree to carry out the Contract under a committee of inspection of his creditors or, being a corporation, shall go into liquidation (other than a voluntary liquidation for the purposes of amalgamation or reconstruction), or if the Contractor shall . . . have an execution levied on his goods . . ."

36. Clause 45 of FIDIC-EMW uses a slightly different wording, and does not grant the purchaser the right to expel the contractor but states that

"[t]he Employer shall be at liberty

"(a) To terminate the Contract . . . if the Contractor shall become bankrupt or insolvent, or have a receiving order made against him, or compound with his creditors, or being a corporation commence to be wound up, not being a members' voluntary winding up for the purpose of amalgamation or reconstruction, or carry on its business under a receiver for the benefit of its creditors or any of them . . ."

37. On the other hand, the contractor may terminate the contract, according to Clause 69.(1) of FIDIC-CEC,

"[i]n the event of the Employer

". . .

"(c) Becoming bankrupt or, being a company, going into liquidation, other than for the purpose of a scheme of reconstruction or amalgamation . . ."

38. In the same situation clause 51.1 of FIDIC-EMW provides that the contractor is entitled to "terminate his employment under the contract".

39. Under the UNIDO-TKL only the insolvency or bankruptcy of the contractor is covered. Article 33.7 permits the purchaser to cancel the contract where the contractor has become insolvent or where he has committed an act of bankruptcy.

40. The FIDIC Conditions contain another ground for termination by the contractor in a situation which amounts in fact to a termination by the purchaser. Clause 69.(1) of FIDIC-CEC entitles the contractor to terminate his employment under the contract

"[i]n the event of the Employer:

". . .

"(d) Giving formal notice to the Contractor that for unforeseen reasons, due to economic dislocation, it is impossible for him to continue to meet his contractual obligations . . ."

41. Clause 51.1 of FIDIC-EMW contains a similar provision without the requirement of a formal notice to the contractor.

### C. Time for termination and procedure to be followed

42. It has been mentioned that in works contracts for the construction of large industrial works the termination is considered as a last recourse in cases of breach of contract. The various clauses dealing with the obligations of the parties contain provisions requesting the creditor to grant to the debtor additional periods of time within which to perform his obligations. It is only at the end of this additional period of grace that the creditor can terminate the contract.

43. Within what period of time after the lapse of such additional period of grace, is the aggrieved party entitled to terminate?

44. Some provisions call for immediate termination after the grounds have been established. On the other hand, in two cases of breach of contract by the contractor or by the purchaser the ECE General Conditions entitle the aggrieved party to terminate the contract without mentioning a time limit (clauses 10.2, 20.5 of both ECE 188A/574A).

45. In the case of non-payment by the purchaser, the contractor is entitled to terminate the contract "within a reasonable time" after the lapse of time mentioned in paragraph 26, *supra* (clause 11.7 of both ECE 188A/574A).

46. Termination "within a reasonable time" is also contained in articles 49 and 64 of the Sales Convention. Such a provision may imply that the creditor loses the right to terminate the contract after the lapse of a "reasonable time".

47. In cases of exonerating circumstances the contract may be terminated "at any time" according to clauses 46.1 of FIDIC-EMW and 65.(6) of FIDIC-CEC. (A similar situation is provided for in article 33.1 of UNIDO-TKL.)

48. The FIDIC-EMW Conditions contain different provisions in case of bankruptcy. If the contractor becomes bankrupt or insolvent the purchaser shall be at liberty "to terminate the Contract *forthwith*" (clause 45), but if the purchaser becomes bankrupt, the contractor is entitled "to terminate . . . by giving 14 days' prior notice" (clause 51.1).<sup>2</sup>

49. In FIDIC-CEC no distinction is made, and for both parties, 14 days' notice is required for termination in case of bankruptcy (clauses 63.(1) and 69.(1)).<sup>3</sup>

50. The requirement of 14 days' notice is also contained in both the FIDIC Conditions in regard to termination (or expelling, see paragraph 11, *supra*) in

<sup>2</sup> The reasons for these different provisions are not clear.

<sup>3</sup> The periods mentioned in paras. 48 and 49 are not periods of grace.



most cases of breach of contract (clauses 44.1 and 51.1 of FIDIC-EMW, clauses 63.(1) and 69.(1) of FIDIC-CEC).<sup>4</sup>

51. The requirement of *one month's* notice is contained in clause 41.3 of FIDIC-EMW in the case of the engineer's failure to issue an interim certificate.

52. Nearly all conditions require the termination to be exercised by giving a *notice in writing* to the other party (for instance clauses 10.2, 11.7, 20.5 of both ECE 188A/574A, all relevant clauses of the FIDIC Conditions).

53. UNIDO-TKL requires a notice in writing in the case of termination (article 33.1 dealing with exonerating circumstances), but no notice need be given in the case of cancellation (article 33.7 dealing with breach of contract by the contractor).

54. All the various clauses of the ECE General Conditions providing for termination include the mention "*without requiring the consent of any court*". This phrase has been added to satisfy the law of some countries (for instance France) where otherwise a termination can be exercised only by resort to a court order.

55. Similarly, article 33.7 of UNIDO-TKL provides that the purchaser can cancel the contract "*without any other authorization*", a wording which might also be aimed at satisfying certain legal systems.

56. The FIDIC Conditions make no reference whatsoever to a court authorization. Attention must be drawn however to the fact that in case of default of the contractor the Conditions provide for the purchaser to enter upon the Site and expel the contractor without voiding the contract. This difference, slight in fact but clear in law, would most likely be interpreted by tribunals as not necessitating a court authorization.

#### D. Consequences of termination

57. Generally, once a contract is terminated the parties must be put in the same stead as at the time of the conclusion of the contract. Sometimes, when the parties cannot be put back in the same position, the contract is terminated for the future only. This last eventuality is the one most often encountered in works contracts in view of their very nature.

58. As termination puts an end to the contract, both parties, as a general consequence, are no longer expected to perform their obligations under the contract. Article 81 of the Sales Convention provides as follows:

"(1) Avoidance of the contract releases both parties from their obligations under it . . ."

59. However, in every contract there are some provisions which should not be nullified by the termination. Termination does not mean the end of all obligations under the contract. Article 81 of the Sales Convention therefore continues:

"Avoidance does not affect any provision of the contract for the settlement of disputes or any other provision of the contract governing the rights and obligations of the parties consequent upon the avoidance of the contract."

60. The parties in particular would not be released from any obligations to pay damages which may be due. Clause 27.1 of both ECE 188A/574A reads as follows:

"Termination of the Contract, from whatever cause arising, shall be without prejudice to the rights of the parties accrued under the Contract up to the time of termination."

61. As far as the other consequences of termination are concerned, the various forms under study distinguish whether termination was caused by breach of contract or exonerating circumstances.

#### 1. Breach of contract

62. Article 20.5 of both ECE 188A/574A provides as follows in case of non-completion:

"... the Purchaser shall be entitled ... to terminate the Contract ... and thereupon to recover from the Contractor any loss suffered by the Purchaser by reason of the failure of the Contractor ... up to an amount ... or ... that part of the price payable under the Contract which is properly attributable to such portion of the Works as could not in consequence of the Contractor's failure be put to the use intended."

63. Clause 31.2 of FIDIC-EMW uses similar language in the case of prolonged delay by the contractor.

64. As mentioned above, under the FIDIC Conditions, when the contractor is in default, the employer may enter the site and complete the work. The wording used in both sets of conditions varies slightly but the outcome is quite similar. Clause 63.(1) of FIDIC-CEC provides in case of default by the contractor:

"the Employer may ... enter upon the Site and the Works and expel the Contractor therefrom without thereby voiding the Contract, or releasing the Contractor from any of his obligations or liabilities under the Contract, or affecting the rights and powers conferred on the Employer or the Engineer by the Contract, and may himself complete the Works or may employ any other contractor to complete the Works. The Employer or such other contractor may use for such completion so much of the Constructional Plant, Temporary Works and materials, which have

<sup>4</sup> The periods mentioned in paras. 50 and 51 have the effect of a period of grace.

been deemed to be reserved exclusively for the execution of the Works, under the provisions of the Contract, as he or they may think proper, and the Employer may, at any time, sell any of the said Constructional Plant, Temporary Works and unused materials and apply the proceeds of sale in or towards the satisfaction of any sums due or which may become due to him from the Contractor under the Contract."

65. FIDIC-CEC Conditions then go on to explain how various questions are dealt with in the event the employer enters on the site and expels the contractor. They read as follows:

*Clause 63.(2)* "The Engineer shall, as soon as may be practical after any such entry and expulsion by the Employer, fix and determine *ex parte*, or by or after reference to the parties, or after such investigation or enquiries as he may think fit to make or institute, and shall certify what amount, if any, had at the time of such entry and expulsion be reasonably earned by or would reasonably accrue to the Contractor in respect of work then actually done by him under the Contract and the value of any of the said unused or partially used materials, any Constructional Plant and any Temporary Works."

*Clause 63.(3)* "If the Employer shall enter and expel the Contractor under this Clause, he shall not be liable to pay to the Contractor any money on account of the Contract until the expiration of the Period of Maintenance and thereafter until the costs of execution and maintenance, damages for delay in completion, if any, and all other expenses incurred by the Employer have been ascertained and the amount thereof certified by the Engineer. The Contractor shall then be entitled to receive only such sum or sums, if any, as the Engineer may certify would have been payable to him upon due completion by him after deducting the said amount. If such amount shall exceed the sum which would have been payable to the Contractor on due completion by him, then the Contractor shall, upon demand, pay to the Employer the amount of such excess and it shall be deemed a debt due by the Contractor to the Employer and shall be recoverable accordingly."

66. According to article 33.7 of UNIDO-TKL, in case of default of the contractor, "the PURCHASER may . . . cancel the Contract and take all or any part of the Contract and/or of the work to be undertaken by the CONTRACTOR out of the CONTRACTOR's hands and may employ such means as the PURCHASER sees fit to complete this Contract and/or the works . . ."

67. In the event the contract is cancelled and the work taken out of the hands of the contractor, article 33 of UNIDO-TKL provides as follows:

"33.8: Where this Contract or any portion or portions thereof has or have been taken out of the

CONTRACTOR's hands . . . the CONTRACTOR shall not . . . be entitled to any further payment including payments then due and payable but not paid and the obligation of the PURCHASER to make payments as provided for in the Terms of Payment shall be at an end, and the CONTRACTOR shall be liable to settle costs and/or damages under the Contract . . .

"33.9: Where this Contract, or any portion or portions thereof has or have been taken out of the CONTRACTOR's hands . . . and is subsequently completed by the PURCHASER . . . the PURCHASER may at its option determine the amount, if any, of retention monies and progress claims of the CONTRACTOR unpaid at the time of taking the work out of the CONTRACTOR's hands that, in the PURCHASER's opinion, are not required by the PURCHASER for the purposes of the Contract and . . . the PURCHASER shall, if of the opinion that no financial prejudice to the PURCHASER will result, authorise payment of that amount to the CONTRACTOR."

"33.10: The taking of this Contract, or of any portion thereof, out of the CONTRACTOR's hands pursuant to this Article does not operate so as to relieve or discharge the CONTRACTOR from the obligations imposed upon the CONTRACTOR by this Contract and by law."

"33.11: If this Contract, the Works, or any part thereof is taken out of the CONTRACTOR's hands pursuant to this Article, all material, plant and interest of the CONTRACTOR in all real property, licences, power and privileges acquired, used or provided by the CONTRACTOR for purposes of this Contract shall be the property of the PURCHASER and in particular, but without affecting any liability or obligation of the CONTRACTOR and/or any PURCHASER right imposed, conferred, or contemplated by any other provision of this Contract, the PURCHASER may, at his option, utilize the equipment or sell or otherwise dispose of, at public auction or at private sale or otherwise, the whole or any portion of such material, and/or plant at such price or prices as he may consider reasonable and retain the proceeds of any such sale or disposition as well as all other amounts then or thereafter due by the PURCHASER to the CONTRACTOR, all in satisfaction or partial satisfaction (as the case may be) of any loss or damage which the PURCHASER has sustained or may sustain by reason aforesaid."

"33.12: Subject to Article 33.11 above, if the PURCHASER considers that any PURCHASER property-interest possessed by virtue of the application of Article 33.11 above, is no longer required for the purposes of the Contract, and that it is not in the interests of the PURCHASER to retain such property-

interest then, upon written notice to such effect from the PURCHASER to the CONTRACTOR, such property-interest shall become the property of the CONTRACTOR."

68. On the other hand, in the event that the contractor terminates the contract the consequences envisaged in the various conditions are different.

69. In such a case the contractor, according to clause 51.2 of FIDIC-EMW, "upon the giving of such notice . . . shall with all reasonable despatch remove from the Site all Contractor's Equipment brought by him thereon." A similar provision is contained in clause 69.(2) of FIDIC-CEC.

70. Clause 51.3 of FIDIC-EMW provides that "[i]n the event of such termination the Employer shall be under the same obligations to the Contractor in regard to payment as if the Contract had been terminated under the provisions of Clause 46 (Outbreak of War) hereof, but in addition to the payments specified in Clause 46.3 the Employer shall pay to the Contractor the amount of any reasonable loss or damage to the Contractor arising out of or in connection with or by consequence of such termination." (The position in clause 69.(3) of FIDIC-CEC is identical.)

71. Termination of the contract by the contractor for breach of contract by the purchaser does not deprive the contractor of any rights already acquired. Thus clause 51.4 of FIDIC-EMW provides:

"Nothing in this Clause contained shall prejudice the right of the Contractor to exercise, either in lieu of or in addition to the rights and remedies in this Clause specified, any other rights or remedies to which the Contractor may be entitled."

72. Under the ECE General Conditions if the contractor terminates the contract for reasons of breach of contract by the purchaser, the contractor is entitled to damages. The General Conditions, however, appear to assume that the parties have agreed to limit the amount of such damages.

73. Clause 10.2 of both ECE 188A/574A in case of not accepting delivery by the purchaser, grants the right to the contractor "to terminate the Contract . . . and thereupon to recover from the Purchaser any loss suffered by reason of such failure . . . or . . . that part of the price payable under the Contract which is properly attributable to such portion of the Plant."

74. In case of non-payment, according to clause 11.7 of both ECE 188A/574A "the Contractor shall be entitled . . . to terminate the Contract and thereupon to recover from the Purchaser the amount of his loss . . ."

75. As long as no assembly or erection on site is involved but only supply of equipment the following provisions of the Sales Convention could well be taken into consideration in regard to works contracts:

*Article 81:* "(2) A party who has performed the contract either wholly or in part may claim restitution from the other party of whatever the first party has supplied or paid under the contract. If both parties are bound to make restitution, they must do so concurrently."

*Article 84:* "(1) If the seller is bound to refund the price, he must also pay interest on it, from the date on which the price was paid.

"(2) The buyer must account to the seller for all benefits which he has derived from the goods or part of them:

"(a) If he must make restitution of the goods or part of them; or

"(b) If it is impossible for him to make restitution of all or part of the goods or to make restitution of all or part of the goods substantially in the condition in which he received them, but he has nevertheless declared the contract avoided or required the seller to deliver substitute goods."

## 2. *Exonerating circumstances*

76. In the event the contract is terminated because of circumstances beyond the control of the parties, clause 25.4 of both ECE 188A/574A provides that "the division of the expenses incurred in respect of the Contract shall be determined by agreement between the parties."

77. And, in the event the parties do not come to an agreement, clause 25.5 provides: "it shall be determined by the arbitrator which party has been prevented from performing his obligations and that party shall refund to the other the amount of the said expenses incurred by the other . . . If the arbitrator determines that both parties have been prevented from performing their obligations, he shall apportion the said expenses between the parties in such manner as to him seems fair and reasonable, having regard to all the circumstances of the case."

78. A formula is provided in clause 25.7 of both ECE 188A/574A to assist the arbitrator in determining the apportionment of liability:

"There shall be credited to the Purchaser against the Contractor's expenses all sums paid or payable under the Contract by the Purchaser to the Contractor. There shall be credited to the Contractor against the Purchaser's expenses that part of the price payable under the Contract which is properly attributable to Plant delivered to the Purchaser or, in the case of an incomplete unit, the value of such Plant having regard to its incomplete state. In either case due account shall be taken of any work done in the erection of such Plant."

79. Where the amount to be credited exceeds the amount of such expenses the party shall be entitled to

recover the excess. "Expenses" means actual out-of-pocket expenses reasonably incurred after both parties shall have mitigated their losses as far as possible. Provided that as respects Plant delivered to the Purchaser the Contractor's expenses shall be deemed to be that part of the price payable under the Contract which is properly attributable thereto, due account being taken of any work done in the erection of such Plant" (clause 25.6 of both ECE 188A/574A).

80. The FIDIC Conditions deal with the consequence of a termination in case of war in the following manner. Clause 46 of FIDIC-EMW provides:

"46.2. . . . the Contractor shall with all reasonable despatch remove from the Site all Contractor's equipment and shall give similar facilities to enable his Sub-Contractors to do so.

"46.3. If the Contract shall be terminated as aforesaid the Contractor shall be paid by the Employer (in so far as such amounts or items shall not have already been covered by payments on account made to the Contractor) for all work executed prior to the date of termination at the rates and prices provided in the Contract and in addition:

"(a) The amounts payable in respect of any preliminary items, so far as the work or service comprised therein has been carried out or performed, and a proper proportion as certified by the Engineer of any such items the work or service comprised in which has been partially carried out or performed.

"(b) The cost of materials or goods reasonably ordered for the Works or for use in connection with the Works which shall have been delivered to the Contractor or of which the Contractor is legally liable to accept delivery (such materials or goods becoming the property of the Employer upon such payment being made by him).

"(c) A sum, to be certified by the engineer, being the amount of any expenditure which in the circumstances was reasonably incurred by the Contractor in the expectation of completing the whole of the Works, in so far as such expenditure shall not have been covered by the payments in this Sub-Clause before mentioned.

"(d) The reasonable cost of removal under Sub-Clause 2 of this Clause and (if required by the Contractor) return thereof to the Contractor's works in his country or to any other destination at no greater cost.

"(e) The reasonable cost of repatriation of all the Contractor's staff and workmen employed on or in connection with the Works at the time of such termination.

"Provided always that, against any payments due from the Employer under this Sub-Clause, the Employer shall be entitled to be credited with any

outstanding balances due from the Contractor for advances in respect of Plant and materials, and any sum previously paid by the Employer to the Contractor in respect of the execution of the Works."

81. Clause 65.(8) of FIDIC-CEC is worded similarly, there is, however, a slight difference in the last paragraph:

"Provided always that against any payments due from the Employer under this sub-clause, the Employer shall be entitled to be credited with any outstanding balances due from the Contractor for advances in respect of Constructional Plant and materials and any other sums which at the date of termination were recoverable by the Employer from the Contractor under the terms of the Contract."

82. The UNIDO model contracts provide, for the event when the contract is terminated by the purchaser because he is subject to any circumstances which are wholly unavoidable and/or beyond his control, as follows (for instance in article 33 of UNIDO-TKL): The contractor shall cease all operations and the purchaser will pay to the contractor an amount equal to the greater of:

*Article 33.3.1:* "The cost of the Works properly supplied or done by the CONTRACTOR as at the date of the termination less all amounts already paid to the CONTRACTOR by the PURCHASER, and less all amounts which the CONTRACTOR is liable under the Contract to pay to the PURCHASER or owing to the PURCHASER, or which the PURCHASER claims is due as damages pursuant to other Articles herein, and

*Article 33.3.2:* "The amount calculated in accordance with the Terms of Payment which would have been legitimately payable to the CONTRACTOR up to the date of Termination provided the CONTRACTOR had in fact fulfilled his contractual obligations to such date, without prejudice to PURCHASER-rights as expressly provided for in this Contract."

83. If the purchaser terminates the contract for reasons of the said circumstances, he has not only obligations vis-à-vis the contractor, but will, according to article 33.5 of UNIDO-TKL, also acquire certain rights:

". . . to obtain from the CONTRACTOR where he is also the Process Licensor the documentation for know-how and basic engineering . . . to receive all detailed engineering documents, calculations, computer printouts and other materials related thereto as completed up to the date of the Termination . . . to receive lists of all equipment for which orders have been placed, together with all copies of Purchase Orders for plant supplied and not supplied . . . to take delivery and receive the shipping papers for all equipment . . . to receive all completed or incomplete

documentation pertaining to work and services . . . to take over the Works including all work done to date on the Site . . . to receive copies of all detailed Civil Engineering, Piping, Instrumentation, lay-out and erection drawings."

### 3. Other grounds for termination

84. Termination by one of the parties as a consequence of a deterioration of the financial situation of the other party is usually treated in the same manner as termination after a breach of contract. For instance clause 45 of FIDIC-EMW provides that if the contractor shall become bankrupt or insolvent the purchaser shall be at liberty to terminate the Contract and to act in the same manner as provided in case of contractor's default.

85. Clause 63.1 of FIDIC-CEC, where the consequence of the contractor's bankruptcy is not termination but that of expelling the contractor, treats this case in the same manner as a breach of contract by the contractor.

86. Under both FIDIC Conditions when the purchaser becomes bankrupt the contractor may terminate and the consequences would be the same as in case of non-payment (clause 51 of FIDIC-EMW, clause 69 of FIDIC-CEC). Similarly, the UNIDO model contracts deal with the question of bankruptcy of the contractor as if it were a breach of contract (article 33.7 of UNIDO-TKL).

## XVIII. APPLICABLE LAW

### A. General remarks

87. In works contracts, parties have an abiding interest in making sure that their rights and obligations are as certain and as predictable as possible. With a view to promoting certainty and predictability and thereby minimizing the possibility of disputes, contract documents usually contain detailed description of the extent of the work to be performed. Disputes, however, do occur and the disputes will have to be resolved in the framework of a legal system or systems. A stipulation of applicable law in the contract by the parties has a great potential for avoiding difficult choice of law problems by the courts.

88. Since the construction of large industrial works is performed over a relatively long period of time subsequent changes in applicable law can produce results which were not contemplated by the parties. Because of these difficulties, parties should try to minimize the chances of recourse to the applicable law by spelling out as fully and as clearly as possible their rights and obligations. Paragraph 45 of the ECE Guide suggests:

"... It may . . . be recommended to the parties . . . to draw up contracts in a sufficiently specific and detailed manner so that, if a dispute should arise, recourse to a national law would be necessary only in exceptional cases."

### B. Choice of applicable law

89. A variety of considerations such as the parties' familiarity with and confidence in the law of a given country may influence the parties' choice of applicable law. The parties are likely to choose one of the following laws: the law of the country where the plant is to be built, the law of the contractor's country, or the law of a third country.

90. Article 36.1 of UNIDO-CRC states some possibilities:

"The laws applicable to the Contract shall be the laws of (*neutral country*) or the law of (*the land where the Plant Site is located*) or as otherwise agreed between the parties in conformity with laws of the country where the Plant is located."

UNIDO-STC and UNIDO-TKL have identical provisions.

91. The counter-proposal does not suggest any applicable law and leaves the matter to the parties:

Article 36.1: "The laws applicable to the Contract shall be . . ."

92. The FIDIC-CEC and FIDIC-EMW make provisions for parties to state the applicable law. Clause 5.1 of FIDIC-CEC provides that there shall be stated in Part II of the Conditions:

"the country or state, the law of which is to apply to the Contract and according to which the Contract is to be construed."

93. Under the ECE General Conditions, the law of the contractor's country is stipulated, subject to a qualification. Clause 28.2 of both ECE 188A/574A provides:

"Unless otherwise agreed, the Contract shall, so far as is permissible under the law of the country where the Works are carried out, be governed by the law of the Contractor's country."

94. The fact that applicable law is stipulated by the parties does not mean it will always be applied by the Courts in which an action is brought. The *lex fori* may restrict the parties' freedom to choose the applicable law.

### C. Additional legal regulations

#### 1. Administrative and other municipal laws

95. The performance of a works contract is a complex undertaking involving, *inter alia*, the supply of

plant and machinery, the construction of the works, the transfer of technology and licensing arrangements. These operations often entail compliance with various laws and regulations in the contractor's and purchaser's countries that are particularly susceptible to governmental economic and social policy. The mandatory requirements of applicable national law in the areas of property rights, patent laws, safety regulations, labour law and currency laws and regulations may affect the performance of the contract.

96. Parties often anticipate and make provision for the effects of municipal law on their contractual obligations. In the forms under study there are express provisions making the contractor responsible for complying with the laws which may apply. Clause 26 of FIDIC-CEC states:

"(1) The Contractor shall give all notices and pay all fees required to be given or paid by any National or State Statute, Ordinance, or other Law, or any regulation, or bye-law of any local or other duly constituted authority in relation to the execution of the Works and by the rules and regulations of all public bodies and companies whose property or rights are affected or may be affected in any way by the Works.

"(2) The Contractor shall conform in all respects with the provisions of any such Statute, Ordinance or Law as aforesaid and the regulations or bye-laws of any local or other duly constituted authority which may be applicable to the Works and with such rules and regulations of public bodies and companies as aforesaid and shall keep the Employer indemnified against all penalties and liability of every kind for breach of any such Statute, Ordinance or Law, regulation or bye-law."

97. If compliance with the law requires payment of fees by the contractor, the contractor is entitled to be reimbursed. Clause 26.3 of FIDIC-CEC provides:

"The Employer will repay or allow to the Contractor all such sums as the Engineer shall certify to have been properly payable and paid by the Contractor in respect of such fees."

98. The wording under FIDIC-EMW is slightly different but the practical effect is the same. Clause 18.1 of FIDIC-EMW states:

"The Contractor shall, in all matters arising in the performance of the Contract, conform in all respects with the provisions of any National or State Statute, Ordinance or other Law or any Regulation or By-law of any local or other duly constituted authority that shall affect the Contractor in the performance of his obligations under the Contract, and shall keep the Employer indemnified against all penalties and liability of every kind for breach of any such Statute, Ordinance, Law, Regulation or By-law."

99. Under the ECE General Conditions, the contractor's responsibility to observe the law applicable to the works is stated by implication. Clause 5.1 of both ECE 188A/574A states:

"The Purchaser shall, at the request of the Contractor and to the best of his ability, assist the Contractor to obtain the necessary information concerning the local laws and regulations applicable to the Works and to taxes and dues connected therewith."

100. The UNIDO model contracts expressly require the contractor to observe all laws that may apply not only to the works but in general. Article 36.2 of UNIDO-CRC states:

"The CONTRACTOR, his staff, and representatives shall observe all codes, laws and regulations in force in the country of the PURCHASER and in the region where the Plant is located."

## 2. Notification of law applicable to the works

101. Construction work is often subject to a wide array of local administrative regulations in connection with performance. The approval of the work plan by the local authority may be hedged around with restrictions relating to health, labour and safety requirements. There may even be requirements relating to equipment, materials and the qualitative level of performance the plant has to meet. The problem here is that in ordinary circumstances, local law is not well known to the contractor.

102. Under some forms under study the party who is more familiar with local laws has an obligation to inform the other of the provisions of local laws and regulations. Frequently the obligation to inform is placed on the purchaser. Clause 18.2 of FIDIC-EMW states:

"The Employer shall give the Contractor assistance to enable the Contractor to ascertain the nature and extent of and to comply with any Laws, Regulations, Orders or By-Laws having the force of law in the country where the Plant is to be erected, which may affect the Contractor in the performance of his obligations under the Contract, and will if so requested procure for the Contractor copies thereof at the Contractor's expense."

103. Under the FIDIC-CEC, the purchaser has no obligation to assist the contractor.

104. The UNIDO model contracts also do not place an obligation on the purchaser to inform the contractor of applicable local laws; the purchaser is however required to provide the contractor with the necessary approvals, permits and licences required by the local authority. Article 5.15 of UNIDO-CRC provides:

"The PURCHASER shall obtain and make available to the CONTRACTOR all necessary permits/approvals and/or licences from local authorities



and/or Government as may be necessary for the timely execution of the Contract inclusive of import licences, visas for CONTRACTOR's personnel, entry permits, work permits, etc."

105. Under clause 5.1 of both ECE 188A/574A, the contractor may request the purchaser for the necessary information on the local laws and regulations that may be applicable to the works.

#### D. Subsequent changes in the laws

106. Even where the parties have taken into account the implications of existing law, their expectations may not be realized because of subsequent changes in the applicable laws. Subsequent changes in the laws may in fact make the performance of the contract unusually burdensome. (For the effects of this situation on the parties' obligations, see part two, XIV, *Renegotiation*.)\*

107. The FIDIC Conditions provide for a revision of the contract price to reflect changes in the law which may affect the performance of the contract. Clause 70.(2) of FIDIC-CEC provides:

"(2) If, after the date thirty days prior to the latest date for submission of tenders for the Works there occur in the country in which the Works are being or are to be executed changes to any National or State Statute, Ordinance, Decree or other Law or any regulation or bye-law of any local or other duly constituted authority, or the introduction of any such State Statute, Ordinance, Decree, Law, regulation or bye-law, which causes additional or reduced cost to the Contractor . . . in the execution of the Works, such additional or reduced cost shall be certified by the Engineer and shall be paid by or credited to the Employer and the Contract Price adjusted accordingly."

108. All UNIDO model contracts have also provided for subsequent changes in the laws which may affect the performance of the work. Article 36.2 of UNIDO-CRC provides:

" . . . In the event that any code, law or regulations are enacted after the Effective Date of the Contract . . . to have adverse effect on the CONTRACTOR's obligations, scope of work, prices and/or time schedule under this Contract, the PURCHASER shall either:

"36.2.1 Obtain appropriate exemption(s) from the relevant authorities on the CONTRACTOR's behalf, or

"36.2.2 Negotiate with the CONTRACTOR for commensurate change(s) in the scope of the work to be

performed under the Contract, together with such changes in price as properly reflect the actual increased costs that are anticipated . . ."

109. Under the counter-proposal the reference point of subsequent changes in the law in force is the date of issue of the invitation to bid.

110. Under the ECE General Conditions, there is also provision for a commensurate adjustment of the contract price. Clause 5.2 of both ECE 188A/574A provides:

"If, by reason of any change in such laws and regulations occurring after the date of the tender, the cost of erection is increased or reduced, the amount of such increase or reduction shall be added to or deducted from the price, as the case may be."

### Part three

#### [A/CN.9/WG.V/WP.4/Add.8\*]

#### LIST OF QUESTIONS FOR POSSIBLE CONSIDERATION BY THE WORKING GROUP

##### A. Introduction

1. General questions concerning the future work of the Working Group have already been described in part one. This part of the study, which identifies specific questions, is not intended to be exhaustive. The questions have to be considered in the context of each of the specific topics under study.

2. It may, however, be emphasized that general questions regarding the methodology for any future work (see part one, paragraphs 39-46) would have to be kept in mind throughout because an adequate formula may be found only after consideration of the specific questions related to each topic.

3. In addition it would be important to point out that the following questions would also be relevant to the entirety of specific questions:

(a) Bearing in mind the various types of contract for the supply and construction of large industrial works (see part one, paragraphs 22-26), can a common approach be adopted for each topic under consideration irrespective of the type of contract, or should different approaches be adopted? Or is there another approach—that a common approach be taken to certain topics, while others have to be tailored to certain types of contract?

\* A/CN.9/WG.V/WP.4/Add.5 (reproduced above).

\* 12 May 1981.



(b) Bearing in mind that there are different types of industrial plant (see part one, paragraph 27), can a common approach be adopted, irrespective of the type of plant involved?

## B. *Specific questions*

### I. *Drawings and descriptive documents*

4. What types of drawings and/or documents should the contractor provide?

5. What should be the legal consequences of failure to provide the drawings and/or documents?

6. Would it be advisable to allow the contractor and/or the purchaser to modify or vary the drawings and/or descriptive documents after the conclusion of the contract?

7. What should be the legal effects of subsequent amendments to drawings and descriptive documents?

8. Should the question of ownership concerning drawings and descriptive documents be dealt with and, if so, which party should be the owner of such documents?

### II. *Supply*

9. Should there be a distinction between the legal position of the contractor and that of the seller in connexion with supply?

10. If the previous question is answered in the affirmative, is the contractor responsible for defects of equipment in individual shipment or for supply of the plant as a whole only?

11. What should be the responsibility of the contractor if he engages a third person to supply the whole or a part of the plant or equipment?

12. Should a provision deal with costs of transportation?

13. If the previous question is answered in the affirmative, what transport is to be arranged by the contractor and what transport costs are to be borne by him?

14. Should the contractor be obliged to supply equipment and/or materials not mentioned in the contract which are, however, necessary for completion of the work, including auxiliary materials and equipment?

15. Should there be a provision in respect of notification of lack of conformity in connexion with supply of plant and legal consequences of failure to notify defects in time?

16. In case of any defects of the materials or the plant supplied by the contractor, is the purchaser to have any remedy in this respect before the date stipulated for

the completion of the work and, if so, what kind of remedies?

17. Should the contractor be responsible for supplies of materials and parts of plant before the date agreed upon for the completion of work and, if so, what should be the legal consequences of failure to supply them?

### III. *Erection*

18. Should the contractor be responsible for the erection of individual parts of the plant or only for completion of the work as a whole within an agreed period of time?

19. If the contractor fails to erect the plant in the agreed time is the purchaser entitled to engage another contractor to do so?

20. What should be the responsibility of the contractor if the personnel of the purchaser or other persons engaged by him participate in the erection of the plant?

21. What should be the extent of the responsibility of the contractor if his undertaking is only in respect of the supervision of the erection of the plant?

22. Should the contractor be obliged to supply all materials and equipment needed for the purpose of erection?

23. Who bears the loss of or damage to materials and equipment mentioned in the previous question?

24. Should the question of co-operation and/or co-ordination between the contractor and the purchaser be regulated and, if so, in what way?

### IV. *Passing of risk*

25. Would it be advisable to determine the legal effects of the passing of risk?

26. If the parties do not agree otherwise, should risk pass at the time of the transfer of ownership to plant or equipment?

27. If the previous question is answered in the negative, would it be preferable to stipulate passing of risk in connexion with supply of individual parts (on "ex works", FOB, CIF, or other bases) or should passing of risk be provided for the works as a whole at a later stage (e.g. completion of the works, take-over or acceptance)?

28. In case the risk is to pass at a later stage (after delivery of individual parts of plant) should certain kinds of risks (e.g. war) pass at an earlier stage?

29. If the plant or equipment or a part of it is lost, destroyed, damaged or deteriorated after the passing of risk, should the contractor, nevertheless, be obliged to cure the defects at the costs of the purchaser?

30. Should there be a provision on risk in respect of materials and equipment used only for construction and not for permanent incorporation into the plant?

31. Should the defects of the plant or of parts of the plant have an effect on the passing of risk and, if so, in what way?

32. Who should bear the risk of transport of defective parts returned to the contractor and of the repaired parts or parts supplied in replacement of the defective parts?

33. Would it be advisable to have a provision on insurance against risk and, if so, to what extent?

34. Should delay in taking delivery have effect on passing of risk?

#### V. *Transfer of property*

35. Is the purchaser to acquire title to the plant:

- (a) Upon its delivery in accordance with the contract;
- (b) Upon delivery to the erection site;
- (c) Upon completion of the works;
- (d) Upon take-over or acceptance;
- (e) Upon payment of the price;
- (f) At some other time?

36. Should an agreement on transfer of property be recognized only if it is in accordance with the law in force in the country where the plant is to be erected?

37. Should the purchaser have a right of detention of the contractor's assets to enforce his rights, if any, in case of breach of contract?

#### VI. *Transfer of technology*

38. Should the contractor be liable to provide the purchaser with know-how relating to the plant to be delivered?

39. If the previous question is to be answered in the affirmative should the obligation of the contractor cover know-how agreed in the contract or the latest know-how available to the contractor at the time of the conclusion of the contract, or at the time when the purchaser is provided with documents relating to know-how?

40. Would the contractor be obliged to supply only technology which is available to him or should the purchaser be provided with technology available to other persons (licensors) as well?

41. Would it be advisable to deal with terms of payment concerning the transfer of technology?

42. Should a provision deal with transfer of technology in connexion with technological developments and improvements in operative techniques after the completion (or take-over or acceptance) of the works?

43. If the previous question is to be answered in the affirmative, should the contractor be obliged to make technological developments and improvements available

to the purchaser free of charge or is the purchaser to pay reasonable costs?

44. Should the purchaser be obliged to supply the contractor with technological developments and improvements in operative technique which the purchaser may discover in connexion with using the work?

45. If so, should the conditions of such transfer of technology be the same as those under which the contractor is obliged to make available the mentioned technological developments and improvements to the purchaser?

46. Should the right of the purchaser to use the transferred technology be limited only to using it in connexion with supplied plant?

47. Would it be useful to have a provision dealing with confidentiality in connexion with transferred technology?

48. In case of such a provision, should there be any exceptions from the principle that the purchaser (contractor) is obliged to treat as confidential the information given to him in connexion with transfer of technology?

49. Should there be a provision on responsibility of the contractor (purchaser) towards the purchaser (contractor) if a third party claims rights based on industrial or other intellectual property in the technology?

#### VII. *Quality*

50. Should there be a provision that all material and workmanship are to conform to the contract or is it advisable to have a specific provision on quality of the plant?

51. In case of such a provision would it be useful to provide for performance standards in a general way (e.g. meeting the full requirements of normal operation, capacity, quality of products and consumption of raw-materials) or should it be preferable to refer to standards and regulations regarding the quality standards of a particular country (e.g. purchaser's country, country in which plant is to be erected)?

52. Is the contractor obliged to conform to a superior standard if required by law of the country in which plant is to be erected and, if so, under what conditions?

53. Should the contractor be obliged to supply other quality if it becomes clear that the quality of plant specified in the contract will not produce a plant capable of performing the intended purpose?

54. If the previous question is answered in the affirmative, who should bear the higher costs caused by a variation of the works?

55. In connexion with the answer to the previous question, should a modification of the works be necessary due to exonerating circumstances?

### VIII. *Inspection and tests*

56. Is the purchaser entitled to examine the plant or equipment and/or materials before their dispatch?

57. If the previous question is answered in the affirmative, what should be the extent of examination? Should provision be made for the place and date of examination?

58. What should the procedure be in respect of examination effected before dispatch of the plant or the equipment?

59. What should be the legal effects of such examination?

60. Who should bear costs concerning examination before dispatch of plant or equipment?

61. What should be the rights and the duties of parties in case of defects in the materials, plant or equipment before their dispatch?

62. Should performance tests be dealt with?

63. If the previous question is answered in the affirmative what provisions should be made regarding:

(a) Pre-conditions for performance tests;

(b) Time of such tests;

(c) Rights and duties of parties in connexion with preparation and execution of such tests;

(d) Procedure to be followed in this respect (including protocol of performance test).

64. Which party is to bear the costs concerning performance tests?

65. What should be the legal effects of successful performance tests?

66. What should be the legal effects if performance tests are not carried out in time?

67. What should be the legal effects if performance tests are not successful?

### IX. *Completion*

68. Is a definition of completion of work needed?

69. If the previous question is answered in the affirmative, what should be the main elements of such a definition?

70. When should the completion period begin to run in case of doubt?

71. Would it be advisable to provide for an estimated period and, if so, how is a fixed period to be determined if parties fail to agree upon it?

72. What should be the legal consequences if no such time is agreed upon in the contract?

73. What should be the legal consequences of completion?

74. Is it advisable to have a provision on prolongation of completion time and if so, under what conditions should such a prolongation be permitted?

### X. *Take-over and acceptance*

75. Should a distinction be made between "take-over" and "acceptance"?

76. What should be the legal consequences of take-over and/or acceptance?

77. Should the purchaser be entitled or obliged to take-over only a part of the works?

78. What should be the legal consequences of such a partial take-over and/or acceptance?

79. What should be the legal consequences of refusal to take-over and/or accept the works?

80. What should be the legal consequences of the purchaser's failure to take-over and/or to accept the works?

### XI. *Delays and remedies*

81. Should delay cover cases where the contractor has not supplied the plant (equipment) and/or has not constructed the works at all or should delay cover partial failure of performance as well?

82. Should delay be considered separately for each part of the installation or is it preferable to take into consideration, in this connexion, only the date of completion of the works as a whole?

83. Should the purchaser have a right to claim performance in case of delay in supply and/or in construction of the works?

84. If the previous question is answered in the affirmative, should such a right be limited as in article 28 of the Sales Convention?

85. As regards questions relating to penalty or liquidated damages, see the Report of the Working Group on International Contract Practices on the work of its second session (A/CN.9/197)\* and the background documents mentioned in paragraph 10 of that Report.

### XII. *Damages and limitation of liability*

86. Are damages to be limited only to direct damage?

87. Should damages include loss of profit?

88. Should the loss which could not reasonably be foreseen by the debtor be excluded from damages?

89. Should any other limitation of damages apply and, if so, to what extent?

90. Should personal injury and/or damage to property not being ordinarily the subject matter of the

\* Reproduced in this volume, part two, I, A.

contract be excluded from the scope of the application of a possible rule?

91. Should the rules on limitation of damages be of an exhaustive nature or should other limitations of damages be admitted on the basis of applicable law?

92. If damages are to be limited by an amount should this amount be stipulated (e.g. by a percentage of price) or is it to be left to the parties to agree upon?

93. Should limitation of damages apply generally or only in certain cases (e.g. termination of contract)?

94. Should the party who relies on a breach of contract be obliged to take measures to mitigate the loss?

95. Should the party in breach of contract claim a reduction in the damages if the party who relies on the breach fails to mitigate the loss?

96. Should there be a distinction between damages in respect of loss caused by delay in performance and loss caused by defective performance?

97. Should damages be excluded in respect of loss caused by defects of materials provided or by a design stipulated by the purchaser?

### XIII. Exoneration

98. Should a possible rule on exoneration be of an exhaustive nature or should other exonerating circumstances be admitted on the basis of applicable law?

99. Should a definition of exoneration be in accordance with the definition of "Exemptions" under article 79 of the Sales Convention or would a different definition be preferable?

100. If a different definition of exoneration is desirable, what elements of the definition of "Exemptions" in the Sales Convention are to be excluded and/or what elements, if any, are to be included?

101. Should exoneration be defined only generally or in terms of a list of exonerating events?

102. If a definition should spell out specific exonerating events, should it be exhaustive?

103. Should the definition cover obstacles of:

(a) A factual nature (e.g. earthquakes) which make performance impossible under all circumstances;

(b) A legal nature (i.e. performance is legally prohibited);

(c) An economic nature (i.e. performance is possible and allowed but at a higher cost, e.g. rising prices of raw materials)?

104. Should the exonerating events be notified?

105. If a notification is to be required, should there be any legal consequences in case of a failure to notify the exonerating event?

106. If so, what are to be legal consequences of such a failure (e.g. loss of right to rely on exonerating events or liability to damages)?

107. Should the legal consequences of exonerating circumstances be limited to the exclusion of damages (as under article 79 of the Sales Convention) or would it be desirable to make further provision for legal effects in connexion with the time for performance or the termination of contract?

108. In case of dealing with the legal effects in connexion with performance time should exonerating events entail an extension of the time for performance or suspension of obligation?

109. If the answer to the previous question is positive, should a time-limit be given for such an extension or suspension?

110. If the termination of contract is to be provided for in connexion with exonerating events, should the person entitled have a right to terminate the contract after a lapse of a certain period of time or should the parties be released from further performance *ipso iure*?

111. Should the right to terminate the contract be limited only to the creditor or should the debtor also be entitled to do so? If so, under what conditions?

112. Should an extension of time for the performance of the contract or the suspension of an obligation to perform or the termination of contract be limited to certain cases only?

113. Should other consequences not mentioned above be included in case of exonerating events?

### XIV. Renegotiation

114. Should a renegotiation clause be limited to exonerating circumstances only or should it cover other cases as well?

115. If so, in what circumstances should there be renegotiation?

116. Should a time-limit be set down for the commencement and the completion of the renegotiation?

117. What factors should be taken into consideration in renegotiation?

118. Should the scope of the provision on renegotiation be limited to certain obligations of the parties (e.g. price revision, extension of time for performance)?

119. Should there be a provision for legal consequences of failure to agree on an adaptation of the contract?

120. If the previous question is answered in the affirmative should either party have the right to terminate the contract or ask a court or an arbitrator to revise the contract?

121. Should the insertion of a hardship clause be encouraged?

122. If such a clause is useful, what changes in circumstances should be covered (e.g. fundamental change, circumstances beyond party's control, substantial economic hardship, etc.); is a period of time to be set down when the clause can be invoked by parties?

123. Should a court, an arbitrator or a third person (chosen by the parties) be entitled to readapt or terminate a contract in the event of hardship?

#### XV. *Guaranties*

124. Should there be a provision on guaranty of workmanship and materials?

125. In case of such a guaranty, is it advisable to limit it or to exclude it in certain cases (e.g. improper use of the plant by the purchaser, defects arising out of materials provided by the purchaser etc.)?

126. What should be the commencement and length of the period of guaranty for workmanship and materials?

127. Should there be a maximum period commencing at the date of delivery?

128. Should the period of guaranty for workmanship and materials be extended by a period during which the works cannot be used by reason of defects covered by the guaranty?

129. What should be the obligations of the contractor if defects appear? Should damages be excluded?

130. What should be the legal consequences if the contractor does not cure the defects in time?

131. Is the purchaser to be given the right to rectify minor defects at the cost of the contractor?

132. Is it advisable to have a provision on performance guaranty?

133. If the previous question is to be answered in the affirmative what should be the content of such guaranty and consequences of its breach?

#### XVI. *Rectification of defects*

134. Should there be different consequences in respect of defects found:

- (a) Before dispatch of the plant (equipment);
- (b) After arrival of the plant or of its parts to the place where the plant is to be erected;
- (c) During construction of the work;
- (d) At the time of completion of the work;
- (e) At the time of take-over or acceptance;
- (f) During the guaranty period;

(g) After lapse of the guaranty period?

135. Is the purchaser to be obliged to notify defects? If so, what is the procedure to be followed?

136. What should be the legal consequences of failure to notify defects by the purchaser (e.g. the right is lost or cannot be exercised)?

137. Should the contractor be obliged to cure the defects of the plant by:

- (a) Replacing the defective plant or parts of it or supplementing missing parts;
- (b) Repairing the defects;
- (c) Granting a price reduction or in another way?

138. Should the purchaser be entitled to choose a form of rectification of defects or should it be the contractor to determine in what way the defects are to be rectified?

139. Should the purchaser be entitled to suspend the work due to its defects and if so, under what circumstances?

140. Should a time-limit be determined for such a suspension?

#### XVII. *Termination*

141. Should the purchaser be entitled to terminate the contract under certain conditions in case of failure of the contractor to complete the works in accordance with the contract?

142. If the previous question is answered in the affirmative, would it be advisable to distinguish between cases where the failure is due to *force majeure* and cases where the contractor is responsible for the failure?

143. Should a distinction be made between cases where the failure of performance by the contractor lies in the fact that he did not supply the plant (equipment) or did not erect the plant and cases where the contractor supplied the plant (equipment) and erected it but with defects?

144. Would it be useful to distinguish between failure to perform in respect of a part of the plant and failure to perform as to the whole of the works?

145. If the contractor fails to perform his obligation to supply and construct the plant should the purchaser be obliged to fix an additional period of a reasonable time for performance in all cases before being entitled to terminate the contract or would it be advisable to grant him a right to terminate the contract under certain conditions (e.g. in case of a fundamental breach of contract) immediately after breach of contract?

146. If the purchaser has the right to declare the contract avoided even in case of a failure of performance regarding a part of the work, should he be entitled to

declare the contract avoided only in respect of the part not performed or the contract as a whole under certain conditions?

147. Would it be advisable to give the purchaser the right to terminate the contract under certain conditions even before the time when the works are to be completed (e.g. if the contractor intimates he will not supply and erect the plant)?

148. Should the right of the purchaser to terminate the contract be limited to certain cases (e.g. fundamental breach of contract)?

149. Should the contractor be entitled to terminate the contract under certain conditions in case of the purchaser's failure to perform his obligation?

150. If the previous question is answered in the affirmative, should such a right of the contractor be limited to:

- (a) Fundamental breach of contract;
- (b) Failure to take over the works;
- (c) Failure to make payment to the contractor in accordance with the contract?

151. If the contractor is entitled to declare the contract avoided, should the principles applicable in respect of right of the purchaser to terminate the contract apply *mutatis mutandis* to such a right of the contractor?

152. What procedure is to be followed as to declaring the contract avoided?

153. Should the contract be terminated in some cases *ipso iure* and if so, under what conditions?

154. Would it be advisable to deal with consequences of termination of the contract?

155. If the previous question is answered in the affirmative, should such consequences be dealt with generally (e.g. to release parties from their obligations to return what has been performed) or in detail?

156. Would it be preferable to maintain the principle that termination of the contract does not affect any contractual provision for the settlement of disputes or any other provision of the contract governing the right and obligations of the parties consequent upon termination of the contract?

157. Should avoidance of the contract exclude the right to claim damages or should it affect the extent to which damages may be claimed?

#### XVIII. *Applicable law*

158. Should there be a provision concerning the applicable law?

159. If the previous question is answered in the affirmative and the applicable law is not chosen by the parties, should the applicable law be that:

- (a) Of the country in which plant is to be erected;
- (b) Of the country in which the contractor has his place of business (or his habitual residence);
- (c) Of the country in which the purchaser has his place of business (or his habitual residence);
- (d) Of the country where the contract was concluded; or
- (e) Of another country?

160. If the local administrative regulations of the country in which the plant is to be erected or in which the purchaser has his place of business (or his habitual residence), are applicable, should the purchaser be obliged to inform the contractor of such rules?

161. If the previous question is answered in the affirmative, what are to be the legal consequences if the purchaser fails to perform his obligation?

162. If the contractor is obliged to comply with the applicable local administrative regulations amended after conclusion of the contract, who is to bear the higher costs?

## 2. NOTE BY THE SECRETARIAT: CLAUSES RELATED TO INDUSTRIAL CO-OPERATION (A/CN.9/WG.V/WP.5)\*

1. The Commission, at its thirteenth session, agreed to accord priority to work related to contracts in the field of industrial development and requested the Secretary-General to carry out preparatory work in respect of contracts on the supply and construction of large industrial works and on industrial co-operation.<sup>1</sup>

2. The Secretariat was not in a position to deal with both subjects at the same time. All the resources available were concentrated on the study related to contracts for the supply and construction of large industrial works.<sup>2</sup>

3. This was, however, not the only reason for not complying with the request of the Commission. The main difficulty for the Secretariat was the fact that it has not a single contract on industrial co-operation in its

\* 7 May 1981. Referred to in Report, para. 75 (part one, A, above).

<sup>1</sup> Report of the United Nations Commission on International Trade Law on the work of its thirteenth session, *Official Records of the General Assembly, Thirty-fifth session, Supplement No. 17 (A/35/17)*, para. 143 (Yearbook . . . 1980, part one, II, A).

<sup>2</sup> A/CN.9/WG.V/WP.4.

possession, and could not, consequentially, analyse international contract practices in this field.

4. At the thirteenth session of the Commission it was noted that the work of the Secretariat would be facilitated if members of the Commission provided the Secretariat with copies of such contracts. By a note-verbale dated 31 October 1980 the Secretary-General solicited the Member States of the Commission to provide copies of such contracts and other relevant materials assuring to keep confidential all materials that are of a confidential nature when received. At the time of the preparation of this note no contract on industrial co-operation has been received by the Secretariat.

5. The main characteristics and contents of an industrial co-operation contract have been described already in a previous study by the Secretary-General.<sup>3</sup> In that study as possible work to be done by UNCITRAL the following was suggested:

"139. In view of the importance of international industrial co-operation and the lack of legal rules the Commission might decide to begin work on industrial co-operation contracts. Elements to be considered could possibly include:

"Interdependence of the constituent parts of industrial co-operation complexes

"Interdependence of the mutual obligations of the parties

"Effects of non-fulfillment of parts of the contract on the matching obligations of the other party

<sup>3</sup> A/CN.9/191, paras. 106-127 (Yearbook . . . 1980, part two, V, B).

"Plurality and change of parties to a contract

"Effects of *force majeure*

"Effects of changed circumstances

"Revision of contracts

"Termination and rescission

"Limitation of damages

"Applicable law

"Settlement of disputes.

"140. The results of the work of the Commission could take the form of model clauses for inclusion in contracts. Also conceivable would be the elaboration of general conditions on international industrial co-operation to be recommended for use by parties to such contracts."

6. As the study of the Secretary-General (A/CN.9/WG.V/WP.4 and Add.1-8)\* reveals, many of the elements noted above can also be found in contracts for the supply and construction of large industrial works. The Working Group, therefore, may wish to consider to concentrate its work for the time being on examination of clauses related to contracts for the supply and construction of large industrial works, and to request the Secretariat to submit, at a future session, a preliminary study on specific features of industrial co-operation contracts when the time appears adequate in the light of progress made by the Working Group on construction contracts.

\* Reproduced in this volume, part two, IV, B, 1.



## V. CO-ORDINATION OF WORK\*

### A. Report of the Secretary-General: current activities of international organizations related to the harmonization and unification of international trade law (A/CN.9/202 and Add.1, 2, 3 and 4)\*\*

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\*\* Referred to in Report, para. 88 (part one, A, above).

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[A/CN.9/202\*]

## INTRODUCTION

1. The United Nations Commission on International Trade Law (UNCITRAL), at its third session, requested the Secretary-General "to submit reports to the annual session of the Commission on the current work of international organizations in matters included in the programme of work of the Commission."<sup>1</sup>

2. In accordance with the above decision reports\*\* were submitted to the Commission at the fourth session in 1971 (A/CN.9/59), at the fifth session in 1972 (A/CN.9/71), at the sixth session in 1973 (A/CN.9/82), at the seventh session in 1974 (A/CN.9/94 and Add.1-2), at the eighth session in 1975 (A/CN.9/106), at the ninth session in 1976 (A/CN.9/119), at the tenth session in 1977 (A/CN.9/129 and Add.1), at the eleventh session in 1978 (A/CN.9/151), at the twelfth session in 1979 (A/CN.9/175) and at the thirteenth session in 1980 (A/CN.9/192 and Add.1-2).

3. At its thirteenth session, the Commission was of the view that the co-ordination of the legal activities of United Nations bodies took on a particular importance at a time when these bodies were increasingly active in the elaboration and adoption of legal rules. It was felt that more information was required about the programmes and terms of reference of the various United Nations organs before it would be possible to recommend a concrete course of action.<sup>2</sup>

4. The Commission therefore requested its Secretariat to submit to it at its next annual session complete information on the activities of other organs and international organizations.<sup>3</sup> In response to the request this report has been prepared for the fourteenth session (1980). In this connexion, it may be noted that a report of the Secretary-General (A/CN.9/203)\*\*\* has also been prepared for the fourteenth session, which in part deals with the question of co-ordination.

\* 26 May 1981.

\*\* Yearbook references for reports mentioned in this paragraph are as follows:

A/CN.9/82: Yearbook . . . 1973, part two, V  
A/CN.9/94 and Add.1-2: Yearbook . . . 1974, part two, V  
A/CN.9/106: Yearbook . . . 1975, part two, VIII  
A/CN.9/119: Yearbook . . . 1976, part two, VI  
A/CN.9/129 and Add.1: Yearbook . . . 1977, part two, VI, A and B  
A/CN.9/151: Yearbook . . . 1978, part two, V  
A/CN.9/175: Yearbook . . . 1979, part two, VI  
A/CN.9/192 and Add.1-2: Yearbook . . . 1980, part two, VI.

\*\*\* Reproduced in this volume, part two, V, B.

<sup>1</sup> Report of the United Nations Commission on International Trade Law on the work of its third session, *Official Records of the General Assembly, Twenty-fifth Session, Supplement No. 17 (A/8017)*, para. 172 (Yearbook . . . 1968-1970, part two, III, A).

<sup>2</sup> Report of the United Nations Commission on International Trade Law on the work of its thirteenth session, *Official Records of the General Assembly, Thirty-fifth Session, Supplement No. 17 (A/35/17)*, para. 149 (Yearbook . . . 1980, part one, II, A).

<sup>3</sup> *Ibid.*, para. 150.

5. The work of the following organizations are described in the present report:

## (a) United Nations bodies and specialized agencies

CTC	Centre on Transnational Corporations A/CN.9/202/Add.1, paras. 62, 65-68
UNCTAD	United Nations Commission on Trade and Development A/CN.9/202/Add.1, paras. 37-38, 53, 71, 76-77, 128 A/CN.9/202/Add.2, paras. 1, 6-8, 11-18, 30-32, 42, 59-63, 128-132
CTN	Commission on Transnational Corporations A/CN.9/202/Add.1, paras. 63-65
ECA	Economic Commission for Africa A/CN.9/202/Add.2, para. 145
ECE	Economic Commission for Europe A/CN.9/202/Add.1, paras. 5-7, 24, 27, 55-59, 129-130 A/CN.9/202/Add.2, paras. 33-35, 40-44, 80, 147-155, 157
ESCAP	Economic and Social Commission for Asia and the Pacific A/CN.9/202/Add.1, paras. 8-10 A/CN.9/202/Add.2, para. 2
ECOSOC	Economic and Social Council A/CN.9/202/Add.2, para. 62
UNESCO	United Nations Educational, Scientific and Cultural Organization A/CN.9/202/Add.1, paras. 98, 108, 114
FAO	Food and Agriculture Organization of United Nations A/CN.9/202/Add.1, paras. 42-45 A/CN.9/202/Add.2, para. 42
GATT	General Agreement on Tariffs and Trade A/CN.9/202/Add.1, para. 29 A/CN.9/202/Add.2, para. 146
UNIDO	United Nations Industrial Development Organization A/CN.9/202/Add.1, paras. 46-47, 58-59
UNITAR	United Nations Institute for Training and Research A/CN.9/202/Add.2, paras. 160-166
IMCO	Inter-Governmental Maritime Consultative Organization A/CN.9/202/Add.1, para. 27 A/CN.9/202/Add.2, paras. 20-22, 24-27, 37, 42

- |       |  |      |  |
|-------|--|------|--|
| ICSID | International Centre for Settlement of Investment Disputes<br>A/CN.9/202/Add.2, paras. 73-75                   | EPO  | European Patent Organization<br>A/CN.9/202/Add.1, para. 119  |
| ICAO  | International Civil Aviation Organization<br>A/CN.9/202/Add.2, paras. 45, 82                                   | EFTA | European Free Trade Association<br>A/CN.9/202/Add.1, paras. 54, 119-121<br>A/CN.9/202/Add.2, para. 133                       |
| ILO   | International Labour Organisation<br>A/CN.9/202/Add.1, paras. 65, 109, 114<br>A/CN.9/202/Add.2, paras. 134-136 | OAS  | Organization of American States<br>A/CN.9/202/Add.1, paras. 60, 69, 81-82, 123, 125, 128<br>A/CN.9/202/Add.2, paras. 86, 159 |
| ILC   | International Law Commission<br>A/CN.9/202/Add.2, paras. 138-144   | OECD | Organisation for Economic Co-operation and Development<br>A/CN.9/202/Add.1, para. 65<br>A/CN.9/202/Add.2, para. 42           |
| WHO   | World Health Organization<br>A/CN.9/202/Add.2, paras. 42, 136  |      |  |
| WIPO  | World Intellectual Property Organization<br>A/CN.9/202/Add.1, paras. 78-80, 84-117, 128                        |      |  |
- (b) *Other international organizations*
- |                                    |  |       |   |
|------------------------------------|--|-------|---|
| AALCC                              | Asian-African Legal Consultative Committee<br>A/CN.9/202/Add.2, paras. 73-75   | IBA   | International Bar Association<br>A/CN.9/202/Add.2, para. 66   |
| CARICOM                            | Caribbean Community<br>A/CN.9/202/Add.2, paras. 96-97  | ICC   | International Chamber of Commerce<br>A/CN.9/202/Add.1, paras. 25-27, 31-33, 36, 131-135<br>A/CN.9/202/Add.2, paras. 8-10, 23, 57, 64-70, 78, 85, 112-117, 121 |
| OCTI                               | Central Office for International Railway Transport<br>A/CN.9/202/Add.1, para. 27   | ICS   | International Chamber of Shipping<br>A/CN.9/202/Add.1, para. 27   |
| CE                                 | Council of Europe<br>A/CN.9/202/Add.1, paras. 14-17<br>A/CN.9/202/Add.2, paras. 104-107, 109-111, 115  | FIATA | International Federation of Freight Forwarders Associations<br>A/CN.9/202/Add.1, para. 27   |
| CMEA                               | Council for Mutual Economic Assistance<br>A/CN.9/202/Add.1, paras. 18-23, 48-52, 118<br>A/CN.9/202/Add.2, paras. 19, 71-72, 156                                    | ILA   | International Law Association<br>A/CN.9/202/Add.2, para. 167  |
| CCC                                | Customs Co-operation Council<br>A/CN.9/202/Add.1, para. 27<br>A/CN.9/202/Add.2, paras. 42, 44  | CMI   | International Maritime Committee<br>A/CN.9/202/Add.1, para. 57  |
| The Hague Conference               | The Hague Conference on Private International Law<br>A/CN.9/202/Add.1, paras. 1, 136<br>A/CN.9/202/Add.2, paras. 77, 84, 108, 121, 158                             | ISO   | International Organization for Standardization<br>A/CN.9/202/Add.1, paras. 27, 30<br>A/CN.9/202/Add.2, para. 42   |
| Inter-American Juridical Committee | <br>A/CN.9/202/Add.1, paras. 70, 83, 122, 124-127  | IRU   | International Road Transport Union<br>A/CN.9/202/Add.1, para. 27<br>A/CN.9/202/Add.2, paras. 42-44  |
| UNIDROIT                           | International Institute for the Unification of Private Law<br>A/CN.9/202/Add.1, paras. 2-4<br>A/CN.9/202/Add.2, paras. 33-39, 46-58, 80-81, 87-95, 98-103, 118-127 |       |   |
| EEC                                | European Economic Community<br>A/CN.9/202/Add.1, para. 27<br>A/CN.9/202/Add.2, paras. 42, 44, 83   |       |   |
- (c) *International non-governmental organizations*
- Institute of International Business Law and Practice  
A/CN.9/202/Add.1, paras. 11-13, 36  
A/CN.9/202/Add.2, para. 79
- (d) *Other organizations*
- Centre for Research on the New International Economic Order  
A/CN.9/202/Add.2, para. 167
- Max-Planck Institute  
A/CN.9/202/Add.1, para. 4

## [A/CN.9/202/Add.1\*]

## I. INTERNATIONAL CONTRACTS

A. *International sales of goods*

1. At its fourteenth session in October 1980, the Hague Conference on Private International Law decided to include in its agenda the revision of the 1955 Convention on the law applicable to international sales of goods. The Secretary-General of the Conference will convoke a special Commission in June 1981 to decide on giving effect to the opening of the Conference for the revision of the Convention to non-member States.

B. *Codification of international trade law*

2. In 1970 UNIDROIT began its work on the elaboration of a code of international trade law. Until now, attention has been concentrated on general principles and a small steering committee prepared the first two chapters of the code dealing with formation and interpretation.

3. These two drafts were submitted to the Study Group on the progressive codification of international trade law at its first session, held in Rome from 10 to 14 September 1979. The attention of the Group was focused principally on the drafts on formation and interpretation in respect of which it was decided that the Secretariat should revise, under the supervision of the Steering Committee, the present text of the two drafts in the light of the proposals for amendment and of the new suggestions made. The Group also agreed that it was opportune to deal in the next chapter of the code with the problem of validity of contracts in general. In this respect it was considered that the work already carried out by the Institute in this field could serve as a starting point and that, in the future draft, specific rules on the validity of general conditions and standard forms of contracts should be added. As to the proposed chapters on performance and non-performance of contracts, it was stressed that these topics, because of their extreme complexity, would need particularly careful preparatory work and the Group requested the President of UNIDROIT to set up special sub-committees for the preparation of the future chapter on performance and non-performance of contracts with which all the interested institutions would be associated.

4. A meeting of an informal working group was accordingly held in Copenhagen on 31 March and 1 April 1980. As regards the future work on validity, the group agreed that this should constitute the third chapter

of the Code and that the basis for the work should be the draft of a law for the unification of certain rules relating to the validity of contracts of international sale of goods approved by the Governing Council of UNIDROIT in 1972 and the comparative study of the Max-Planck Institute on which that draft had been based. The provisions of the 1972 draft would have to be revised so as to render them applicable to commercial contracts in general and the comparative study updated to take account of the latest developments, in particular those in the Socialist countries which had recently adopted special rules for international commercial contracts. The group further decided that some additional rules should be included in the 1972 draft regarding the illegality, immorality and unfairness of contracts, in addition to the classical hypotheses of invalidity of contracts, i.e. mistake, fraud and duress already dealt with therein. In respect of the chapter of the Code relating to performance and non-performance, it was decided that a first study should deal with the topics of performance and specific performance, a second with the question of rescission and damages and a third with other remedies. The group reviewed the progress so far accomplished at a second session held at Hamburg in February 1981.

C. *Counter-trade practices*

5. A notable development in international trade during recent years has been the increasing frequency of transactions based on arrangements through which specific interlinkages are established between sales and purchases. Although counter-trade arrangements are by no means a new phenomenon, difficulties in recent times in financing trade through conventional commercial transactions have prompted increasing recourse to counter-trade for financing purposes and as a means of facilitating access to markets and overcoming trade obstacles. This tendency has taken on special prominence in east-west trade. Counter-trade also occurs, however, in commercial relations between countries belonging to the same economic groupings and in relations between ECE member countries and developing countries.

6. The ECE Committee on the Development of Trade decided at its twenty-seventh session in 1978 to invite the Secretariat to undertake a study that would define and describe the use of counter-trade practices (CTP) in the ECE region for submission to the twenty-eighth session of the Committee in 1979. Its purpose can be defined as follows:

To describe, analyse and, wherever possible, quantify the various kinds of counter-trade practices conducted in the ECE region;

To examine the motives of enterprises' and organizations' participation in the various forms of counter-trade;

\* 6 May 1981.

To analyse the institutional and organizational arrangements whereby these transactions are conducted;  
To assess trends.

7. A paper was prepared by the Trade and Technology Division for the Committee on the Development of Trade entitled "Counter-trade practices in the ECE region" (TRADE/R.385 and Add.1, 2 and 3). The study is in two parts: (a) the form and scope of counter-trade in the ECE region; and (b) policies and practices in this field. Part one contains a typology of counter-trade arrangements, a description of the main practices encountered in the ECE region and a brief assessment of trends in various sectors. Part two deals with policies at the national and international levels in the field of counter-trade, and examines the role and the motives of enterprises and organizations engaged in this type of activity. Contractual and financial aspects are also dealt with in the second part of the study.

#### D. *Contract forms, standard and model contracts and general conditions*

##### 1. *Contract form for pepper*

8. The ESCAP International Trade Division's project entitled "Development of common sales contract form for pepper" was approved for implementation in mid-1980. This project is aimed at increasing the stability of the pepper trade and also protecting the interest of pepper producing countries by utilizing a new uniform contract form for pepper. The proposed new contract form will, as a minimum, embody the following clauses or provisions:

Various bases for sales, i.e. CIF, C and F, spot, future delivery;

Weight and quality assessment, inspection and certification at both the shipping and receiving end by government/independent authorities;

Commercial arbitration procedures equitable to both sellers and buyers, including national litigation procedures;

Payment terms, delivery and acceptance;

Relief methods in case of default;

Penalty for presentation of dubious or falsified claims over quality or quantity;

Confiscation, detention and rejection of consignments;

Damage, loss etc., and non-compliance or partial fulfilment of contract;

Fluctuation in exchange rate of the currency used in the contract and also the export duties imposed by exporting countries where applicable;

Rights and liabilities of contracting parties.

9. A consultant was recruited by the ESCAP secretariat early in 1981 to draw up a draft contract form after examining various existing forms and holding discussions with exporters and relevant government agencies involved in the pepper trade in the International Pepper Community member countries in the ESCAP region, namely, India, Indonesia and Malaysia. The study will be undertaken in mid-1981, and the results of the study will be presented to the meeting of the International Pepper Community Permanent Panel on Techno-Economic Studies to be held in late 1981.

##### 2. *Standard contracts/general conditions for tropical hardwood trade*

10. As part of the technical assistance programme for the tropical timber producing developing countries in the region, the International Trade Division of ESCAP has been carrying out a study on the development of standard contracts and general conditions to be used in the tropical timber trade in the region. This study is part of the project entitled "Development of standard contracts/general conditions and formulation of uniform gradings rules and specifications for tropical hardwood trade in the ESCAP region". The study will comprise a comprehensive review of existing trade practices obtained in the business sector regarding tropical logs, sawn timber, veneer and plywood. Fact-finding missions to a number of tropical timber producing and consuming countries within and outside the region were undertaken early in 1979. Consultations were held with government agencies, timber associations, chambers of commerce and other international agencies. The study, along with the draft standard contracts/general conditions, will be presented to an intergovernmental meeting of tropical timber producing countries scheduled to be held in June 1981.

##### 3. *Cost plus fee contracts*

11. The Institute of International Business Law and Practice will undertake a study on "cost plus fee contracts" (Document 400/94a). Under the traditional type of contract for civil engineering, the general contractor agrees to complete works in accordance with the client's specification for a lump sum. It is then up to him to execute the contract and to take the risks of cost escalation.

12. The "cost plus fee" contract alters the relationship between client and general contractor in a number of ways. The general contractor does not take the risk of cost inflation and instead of the profit margin between lump sum and costs he is remunerated by fixed fee. There is a different distribution of responsibilities between client and contractor who becomes much more of a project manager on the client's behalf.

13. The research project aims to study the operation of cost plus fee contracts and to analyse standard clauses. It will make recommendations to assist all those concerned in drafting such contracts. The working party will be made up of lawyers, accountants and engineers.

#### 4. "Standard" contracts

14. One of the proposed subjects for inclusion in the CE Medium-Term Plan 1981-1985 is standard contracts. To some extent, the problems posed by so-called "standard" contracts (*contrats d'adhésion*), i.e. contracts or contract clauses drafted in advance and *ne varietur* by one of the parties, or by a person other than one of the contract parties (e.g. a professional body), and proposed ready-made to any person interested in a given transaction, have already been dealt with in connection with unfair terms in consumer contracts (Resolution (76) 47 of the Committee of Ministers).

15. However, this type of contract raises a number of questions that might well be considered at international level, particularly in view of the increasingly frequent use of such contracts in international transactions. The issues that might be investigated include the legal nature of such contracts, conclusion of such contracts, acceptance and interpretation of standard terms, etc.

#### 5. Publishing contracts

16. One of the proposed subjects for inclusion in the CE Medium-Term Plan 1981-1985 is publishing contracts. Publishing is becoming increasingly international. This entails the need for an effort to bring national laws into line, or at least to seek a common solution to the international problems arising in the field.

17. The Benelux countries have already worked on this problem. Since two different systems of law had to be taken into account in the Benelux countries (Belgium-Netherlands), this work could serve as a model, core and starting point for an attempt to co-operate on a wider scale, through CE.

#### 6. General conditions governing technical standards of maintenance of machines, equipment and other goods

18. These were prepared by the CMEA Executive Committee in 1973. They apply to all contracts for technical maintenance concluded between organizations of CMEA member countries empowered to conduct foreign trade operations. In accordance with a decision of the CMEA Executive Committee, the Standing Commission on Foreign Trade is drafting proposals for improving the General Conditions referred to above.

#### 7. General conditions of delivery of goods

19. The work of the CMEA organs on the standard-

ization of regulations covering foreign trade deliveries has gone through several stages. The first stage of this work in the framework of CMEA involved the preparation of a model document pertaining to "General Standardized Commercial Conditions relating to Contracts for Reciprocal Deliveries of Goods between Countries Participating in the Council" (GCD CMEA 1955). CMEA recommended that member countries should adopt these conditions to govern reciprocal deliveries. Bilateral agreements pertaining to the general conditions to govern deliveries were concluded on the basis of this recommendation between participant countries. The second stage comprised the preparation and implementation of a common multilateral document entitled "General Conditions Governing Delivery of Goods between Foreign Trade Organizations of Countries Participating in the Council (GCD CMEA 1958). The third stage in the work of standardization was the approval by the CMEA Standing Commission on Foreign Trade in June 1968 of the improved "General Conditions Governing Delivery of Goods among Organizations of CMEA Member Countries" (GCD CMEA 1968), which were brought into operation on 1 January 1969.

20. The approval of GCD CMEA by the Standing Commission on Foreign Trade in 1968 made it possible to achieve a high degree of standardization of regulations governing relations between organizations in CMEA member countries in the sphere of foreign trade deliveries. However, several matters relating to contractual obligations have still to undergo standardization.

21. After adoption of the Comprehensive Programme, further work was undertaken within the framework of CMEA on matters which did not achieve uniform settlement in GCD 1968 related to the liability of economic organizations for failure to comply with or inadequate compliance with their mutual obligations. As a result, in 1975 and 1979, on the recommendation of the CMEA Standing Commission on Foreign Trade, changes to GCD 1968 proposed by the CMEA Conference on Legal Matters were approved by the CMEA Executive Committee.

22. GCD CMEA 1968/1975, in the 1979 version, has been applied since 1 January 1980. It serves as the basis for the settlement of practically all questions related to the conclusion and implementation of contracts covering deliveries of goods between organizations in the member countries of CMEA.

23. A study is currently being undertaken within the framework of the CMEA Conference on Legal Matters of practice and experience in the application of GCD CMEA 1968/1975 in the 1979 version. The aim of the study is to draw up possible proposals for the further improvement of GCD CMEA and/or its practical application.



## 8. *General conditions of sale of milk*

24. The ECE Committee on Agricultural Problems (Working Party on Standardization of Perishable Produce) is engaged in a project for the establishment of standard documents for general conditions of sale for milk and milk products with emphasis on current trade practices in Europe but with regard to potential usefulness in other regions. Technical regulations and rules on safety of products and surveillance will be included. Legal issues concern, *inter alia*, responsibility of contracting parties, products liability, payments, trade documents, claims and arbitration. All these relate to private international law. The project is being implemented in co-operation with the International Dairy Federation (IDF-FIL). The general conditions will be available for use by the trade and will have the legal force of a recommendation. The general conditions have not yet been adopted.

### E. *International trade terms and standards*

#### 1. *Incoterms*

25. The revision of Incoterms by the ICC Commission on International Commercial Practice came into force on 15 March 1980 (ICC Publication No. 350). The revision was made following the analysis of the problems resulting from the changes which have occurred in transportation techniques, legal practices and documentary procedures, creation of two new terms "Free carrier" and "Freight (or carriage) and insurance paid to" and revision of the term "Freight (or carriage) paid to".

#### 2. *Terms dealing with containerized and combined transport*

26. ICC is continuing its study of the drafting of terms dealing with containerized and combined transport (Document No. 460/179 and Document No. 460/INT. 106).

#### 3. *Coding terms of payment*

27. The ECE Committee on the Development of Trade (Working Party on Facilitation of International Trade Procedures) is engaged in a project which contains mnemonic acronyms, designed on the same principal as the Incoterms, of main terms of payment relating to a contract of sale. The text of the Recommendation (No. 17) was adopted by representatives of the following ECE countries who attended the twelfth session of the Working Party on Facilitation of International Trade Procedures: Austria, Belgium, Bulgaria, Canada, Czechoslovakia, Denmark, Finland, France, German Democratic Republic, Germany, Federal Republic of,

Hungary, Netherlands, Norway, Poland, Romania, Spain, Sweden, Switzerland, Turkey, USSR, United Kingdom, and the United States. Also present were representatives of the following governmental and non-governmental organizations: Inter-governmental Maritime Consultative Organization (IMCO), European Economic Community (EEC), Customs Co-operation Council (CCC), Central Office for International Railway Transport (OCTI), International Chamber of Commerce (ICC), International Road Transport Union (IRU), International Union of Railways (UIC), International Organization for Standardization (ISO), International Chamber of Shipping (ICS), International Railways Transport Committee (CIT), International Federation of Freight Forwarders Associations (FIATA), and International Union of Combined Rail/Road Transport Companies (UIRR).

28. The Recommendation TRADE/WP.4/R.102 mainly concerns:

Buyers and sellers in their mutual relations regarding a sale contract;

Government bodies responsible for exchange control and statistics.

#### 4. *GATT standards code*

29. At the end of 1979, the GATT standards code was published—giving a strong governmental support for voluntary standardization at the international level. Differences in national laws, regulations and standards are frequently obstacles to a free trade between countries. In order to eliminate those technical barriers to trade, there is a need for more international product standards that can be used as a basis for national laws and regulations. This is the major conclusion drawn in the "Standards Code", now agreed within GATT (the General Agreement on Tariffs and Trade), and which will serve as a guiding rule for governmental standards policy. GATT sees international standardization as a major instrument in the harmonization of what has been done, and what will be done, at the national level. The GATT standards code relates primarily to product standards. ISO is also intensifying its work in the field of product specifications.

#### 5. *International standards*

30. In May 1980, the total number of ISO International Standards reached 4,000. In addition, there are now more than 3,500 draft standards in preparation as international trade has grown considerably. The scope of ISO has widened considerably. Thirty-nine ISO technical committees have been created, over the past ten years, for such new areas as implants for surgery, ergonomics, medical equipment, agricultural products and jewellery.

## F. Model clauses

### 1. Force majeure and hardship clauses

31. The Working Party "Contracts" was set up in 1977 within the ICC Commission on International Commercial Practice with a view to making a comparative analysis of the current conceptions held by national laws regarding the concept of *force majeure* and the hardship theory and to drafting clauses which provide for the adaptation of the contract to changed circumstances for insertion in contracts to be performed by stages concluded on a more or less long-term basis or else contracts with performance deferred for a period of time.

32. A draft model contract clause on release from liability was drawn up on the basis of a revised report by Professor Van Ommeslaghe (Document No. 460/233) and the results of the discussions within the Commission (5 June 1980, Document No. 460/253) and the working party (16 September 1980, 13 November 1980, Document No. 460/262). The clause on release from liability distinguishes between the event of *force majeure* defined according to a strict conception and the circumstances releasing from liability as contractually stipulated by the parties regardless of whether such circumstances had the character of an event of *force majeure*. An indicative enumeration of such circumstances was provided, it being understood that it was up to the parties to adapt this list to their needs.

### 2. Limited liability clauses

33. The ICC Working Party "Contracts" set up within the ICC Commission on International Commercial Practice will be initiating in 1982 a project on model contractual clauses limiting the liability of the parties to a contract in the case of loss to one of them by setting a maximum compensation if the liability is ascertained under the terms of these clauses.

### 3. Penalty clauses

34. A study is undertaken on penalty clauses by the "Contrats internationaux" study group created under the aegis of *droit et pratique du commerce international*; the UNCITRAL Secretariat maintains close contact with the Group in relation to the project on liquidated damages and penalty clauses presently undertaken by the UNCITRAL Working Group on International Contract Practices.

### 4. Terms of avoidance in contracts

35. One of the proposed subjects for inclusion in the CE Medium-Term Plan 1981-1985 is terms of avoidance in contracts. Contracts of a variety of types may contain terms of avoidance (contracts of sale, leases, employment contracts, service contracts etc.).

## G. Trade usages

36. The Institute of International Business Law and Practice is undertaking a project on the interpretation and application of international trade usages (Document 400/94). The essence of international trade usages is that they represent a universal practice adapted to business requirements in a particular trade. The study will examine court decisions affecting international trade usages and will propose by the ICC or other bodies if this is required.

## II. COMMODITIES

### A. Commodity agreements

37. Pursuant to paragraphs 3(e) and 23(a) of General Assembly resolution 1995 (XIX), as amended, and Conference resolutions 93 (IV) and 124 (V) on the integrated programme for commodities, one of the major responsibilities of UNCTAD is the preparation and negotiation of international agreements in the field of commodity trade.

38. In the years 1977-1980 the following international agreements were adopted by United Nations conferences held under the auspices of UNCTAD:

International Sugar Agreement, 1977 (Document TD/SUGAR.9/12)

International Olive Oil Agreement, 1979 (Document TD/OLIVE OIL.7/7/Rev.1)

International Natural Rubber Agreement, 1979 (Document TD/RUBBER.15/Rev.1)

International Cocoa Agreement, 1980 (Document TD/COCOA.6/7)

Agreement Establishing the Common Fund for Commodities (Document TD/IPC/CF/CONF/24).

39. The Agreement Establishing the Common Fund for Commodities, when it enters into force, will establish a new multilateral financial institution of a universal character aimed at facilitating the conclusion and functioning of International Commodity Agreements, particularly concerning commodities of special interest to developing countries. Its functions will include the financing through its first account of commodity stocks and through its second account of commodity development measures.

40. The United Nations Tin Conference has been convened to prepare and adopt the (sixth) International Tin Agreement. The United Nations Conference on Jute and Jute Products has been convened to prepare and adopt an International Agreement on Jute and Jute Products.

41. It is expected that other international instruments will be drawn up pursuant to Conference resolutions 93(IV) and 124(V) on the Integrated Programme for Commodities.

#### B. *Informal commodity arrangements and guidelines*

42. The FAO Intergovernmental Commodity Groups generally follow a voluntary consultative approach in seeking solutions to commodity problems. These specialized commodity groups, comprising interested producing and consuming countries have continued to meet in order to identify specific commodity problems and to mitigate them through informal arrangements or guidelines to provide a code of conduct for producing and consuming countries, particularly with reference to international trade. Recently four of the groups have been successful in reaching the agreements set forth below.

##### *Informal price arrangements on hard fibres*

43. The informal price arrangements on hard fibres cover sisal and abaca and aim at the stabilization of prices and trade of these commodities. The arrangements are operated under the FAO Intergovernmental Group on Hard Fibres comprising 60 governments. The Group reviewed the arrangements in February 1980 and agreed to raise the indicative price range of East African U.G. sisal. In the past, the arrangement on sisal has provided also for export quotas but the Group agreed that these should remain suspended. Further, since the prices of abaca in early 1980 were well above the ceiling set by the Group in September 1979, it decided to suspend temporarily the trigger mechanism for the automatic consultation provided for under the informal indicative price arrangement for abaca.

##### *Informal price arrangements on jute, kenaf and allied fibres*

44. Informal price arrangements on jute, kenaf and allied fibres aim at alleviating severe difficulties facing the jute trade because of sharp fluctuations in prices of these commodities. The FAO Intergovernmental Group on Jute, Kenaf and Allied Fibres which has a current membership of 47 Governments, reviewed the arrangements in October 1979 and decided to keep the indicative price range for jute for 1979-1980 at the 1978 level and to raise the price range for Thai kenaf.

##### *International guidelines*

45. As an alternative to formal commodity arrangements, FAO Intergovernmental Groups have evolved International Guidelines to provide a "code of conduct" for the achievement of agreed goals. The following Guidelines have been drawn up recently:

##### *Guidelines on rice*

The FAO Intergovernmental Group on Rice, having a membership of 82 countries, adopted in March 1980 an Informal and Voluntary Framework for International Consultations on Rice. This includes the revised and strengthened Guidelines on National and International Action on Rice adopted by the Group in November 1979. The Framework aims at achieving a balanced situation in production, consumption and trade in rice and at ensuring orderly trading taking into account the interests of developing countries. It contains guidelines for concessional transactions and provides for the review by the Group of rice production programmes and the evaluation of rice stocks for world food security. The text of the Framework is contained in the report of the twenty-third session of the Group (March 1980) and the Revised Guidelines are in the report of the twenty-second session (March 1979).

##### *Guidelines on oilseeds, oils and oilmeals*

The Intergovernmental Group on Oilseeds, Oils and Fats with a membership of 88 countries, adopted in April 1980 the Guidelines for International Cooperation in the Oilseeds, Oils and Oilmeals Sector with the main aim of harmonizing national policies in the light of agreed objectives for the world oilseeds, oils and oilmeals economy. The text of the Guidelines is contained in the report of the fourteenth session of the Group held in April 1980.

### III. INDUSTRIALIZATION

#### A. *UNIDO model contracts for the fertilizer industry*

46. UNIDO is engaged in drafting the following model contracts for the fertilizer industry:

Second Draft of the UNIDO Model Form of Turn-Key Lump-Sum Contract for the Construction of a Fertilizer Plant (ID/WG.318/1)

First Draft of the UNIDO Form of the Semi-Turn-Key Contract for the Construction of a Fertilizer Plant (ID/WG.318/2)

Third Draft of the UNIDO Model Form of Cost Reimbursable Contract for the Construction of a Fertilizer Plant (ID/WG.318/3).

47. The above Drafts were submitted to the Third Consultation on the Fertilizer Industry at São Paulo, Brazil, held from 29 September to 2 October 1980 (there was an earlier meeting in November 1978, see A/CN.9/WG.V/WP.4,\* paragraphs 10 and 11). The Drafts are expected to be finalized at the end of 1981.

\* Reproduced in this volume, part two, IV, B, 1.

### B. *Industrial, scientific and technical co-operation*

48. The CMEA Committee on Scientific and Technical Co-operation drafted a document on organizational, methodological, economic and legal principles for scientific and technical co-operation among CMEA member countries and for the activities of CMEA organs in this field. This was approved by the CMEA Executive Committee in 1972. Proposals for changes or additions to the document referred to above are now being drafted on the basis of experience accumulated during its implementation.

49. Model clauses for agreements concerning scientific-technical co-operation and a model agreement covering work of this kind were prepared by the CMEA Conference on Legal Matters in 1975. Model agreements concerning the creation of a temporary international scientific-technical team and the setting up of a joint laboratory (department) were drafted in 1977.

50. The CMEA Conference on Legal Matters has embarked upon the drafting of model rules concerning the liability of organizations for failure to comply with or inadequate compliance with obligations arising from contractual relations in the field of scientific-technical co-operation. Preparation has begun of a model agreement on the execution of commissioned research, design and experimental work.

51. The CMEA Conference on Legal Matters drafted General Conditions for Specialization and Co-operation in Production between CMEA Member Countries. These were approved in 1979 by the CMEA Executive Committee, which recommended the member countries of CMEA to implement the General Conditions mentioned above as of 1 January 1980.

52. In line with the work plan and programme of the CMEA Conference on Legal Matters, a study of the legal questions associated with multilateral inter-State relations in the realm of specialization and co-operation in production is currently being carried out. A study is also envisaged on contractual practice in the field of specialization and co-operation in production between the organizations of CMEA member countries.

53. In the execution of technical assistance projects, UNCTAD has been involved in projects for the preparation of treaties for integration groupings of developing countries and on regimes for multi-national enterprises of such groupings.

54. In the framework of the Joint EFTA-Yugoslavia Committee, a group of legal experts on model contracts for industrial co-operation has been established. Its task is to "seek within the frame of the relevant legislation in the countries concerned and taking into account the realities of industrial co-operation transactions, solutions which are of interest in the present context and which clearly define the right and obligations of the enterprises

participating in such transactions and elaborate models for different forms of contracts". The group held its first meeting in January 1981.

### C. *Draft guide for drawing up international contracts on consulting engineering, including related aspects of technical assistance*

55. At its fifteenth session held from 26 to 28 November 1979, the ECE Group of Experts on International Contract Practices in Industry (Committee on the Development of Trade) requested the Secretariat to prepare for first reading at, and submission to, its sixteenth session, a draft document on drawing up international contracts on consulting engineering, including related aspects of technical assistance, based on an outline of international engineering contracts (TRADE/GE.1/R.21) and List of Topics (TRADE/GE.1/CRP.37/Rev.1); to draw up a list of model contracts, guides and general conditions used in the preparation of the draft document. It was agreed that the draft document should comprise consulting engineering only and should closely resemble the format of a Guide on drawing up international contracts in this field (referred to as the "draft Guide").

56. The objective of this project is to assist clients and their lawyers in the drafting of international contracts on consulting engineering including related aspects of technical assistance.

57. In April 1980 the secretariat completed the first draft of the Guide. During the sixteenth session (14-16 July 1980), it was decided that the draft Guide should be descriptive rather than prescriptive, should include references to general international practice and consequences, and—except in its introduction—should avoid references to complex engineering. In the light of comments, the Group of Experts made suggestions concerning redrafting the existing text by the secretariat. It prepared a revised version of the draft Guide (TRADE/GE.1/R.22/Rev.1) for the seventeenth session held on 15-17 December 1980.

### D. *Publication*

58. A Study on International Industrial Co-operation was launched initially by UNIDO in response to resolution 3362 (S-VII) of the Seventh Special Session of the United Nations General Assembly held in September 1975. Paragraph 7, part IV of resolution 3362 stated: "A joint study should be undertaken by all Governments under the auspices of the United Nations Industrial Development Organization, in consultation with the Secretary General of the United Nations Conference on Trade and Development, making full use of the knowledge, experience and capacity existing in the United Nations

system of methods and mechanisms for diversified financial and technical co-operation which are geared to the special and changing requirements of international industrial co-operation. A progress report on this study should be submitted to the General Assembly at its thirty-first session." A meeting of eminent persons was held by UNIDO at Vienna in June 1979 and at a United Nations Inter-Agency Meeting in July 1979. The final draft of the Study was considered at the Third General Conference of UNIDO held in January and February 1980, at New Delhi, India.

59. The final draft of the Study, renamed "Industry 2000—New Perspectives", is based on the fundamental principle that the restructuring of the world economy must assume, and in fact coincide with, the restructuring of world industry. Specific mechanisms for accelerating international resource flows within and to the South were presented as concrete steps towards reaching the Lima target for industrialization of the third world and building a new international economic order.

60. The Inter-American Juridical Committee of OAS in its session in 1972 included the topic "Treatment of the foreign instruments" in its agenda. Subsequently, the General Secretariat of the OAS prepared some documents on foreign investments, among them was the document issued in 1975, entitled "Comparative Study of Latin-American Legislation on the Regulation and Control of the Private Foreign Investment". The study considers the legislation of the Latin American countries in force on 30 December 1974. Other topics have also been considered in the above study, such as the institutionalization of the mechanisms of control, utilization of internal credit, utilization of external credit; transfer of technology, transfer of profits, reinvestment of profits and repatriation of funds.

61. A supplementary study on foreign investment was prepared in June 1977 by the General Secretariat. This supplement points out the new trends of foreign investment in Latin America in recent years. It refers to the new legislation of Argentina and Chile on this matter, as well as the changes introduced by the Commission of the Cartagena Agreement to the Common Regime of Treatment of Foreign Investment.

#### IV. TRANSNATIONAL CORPORATIONS

##### A. *Role of transnational corporations*

62. CTC in response to General Assembly resolution 33/198 of 29 January 1979 inviting "the governing bodies of the organs and organizations concerned within the United Nations system to assess, within their respective areas of competence, the progress made towards

the establishment of the new international economic order, as well as to indicate the obstacles that impede its establishment, . . . with a view to submitting comprehensive reports to the Assembly at its special session in 1980" prepared a report entitled "Progress made towards the establishment of the new international economic order: the role of transnational corporations" (E/C.10/74 and Corr.1). The report first documents the approach of the programme for the new international economic order towards transnational corporations and relates it to the thrust of that programme to bring about the structural changes that are needed to allow self-sustained development. It then examines progress made in recent years in terms of changing patterns of interactions, in reference to transnational corporations, between the developed and the developing countries and in terms of strengthening the capacity of developing host countries to deal with transnational corporations. In a concluding section, some tentative conclusions are drawn regarding the role of transnational corporations in the establishment of the new international economic order. This report was submitted to the General Assembly at its eleventh special session for consideration.

##### B. *Code of conduct*

63. The Intergovernmental Working Group on a Code of Conduct on Transnational Corporations was established by CTN at its second session held from 1 to 12 March 1976. A first draft of the Code should be completed before the seventh session of the Commission in 1981 (18-28 May 1981).

64. At its eighth session (7-18 January 1980), the Working Group requested the chairman to prepare formulations on the implementation of the Code including relevant aspects of intergovernmental co-operation (E/C.10/AC.2/14). The matters dealt with in the Code include respect for national sovereignty and observance of domestic laws, regulations and administrative practices, adherence to economic goals and development objectives, policies and priorities; adherence to socio-cultural objectives and values, respect for human rights and fundamental freedoms, non-interference in internal political affairs, non-interference in intergovernmental relations, abstention from corrupt practices, ownership and control, balance of payments and financing transfer pricing, taxation, competition and restrictive business practices, and employment and labour (E/C.10/62 Annex) (9 June 1980).

##### C. *Principles concerning multinational enterprises*

65. Subsequent to the examination of the first reports of Governments on the effect given to the Tripartite Declaration of Principles concerning Multi-

national Enterprises and Social Policy (adopted in 1977), the Governing Body of ILO on 19 November 1980 adopted provisions concerning further follow-up procedures. One of the provisions so adopted specifies that ILO should retain sole responsibility for the implementation and interpretation of the Declaration, while ensuring appropriate co-ordination with the United Nations and other organizations. Close working relationships in this area have been established with CTC, CTN and its intergovernmental working group, on the one hand, and with the competent services of OECD on the other.

#### D. Publication and research

66. CTC's activities have been principally geared to the development of an infrastructure, within which a comprehensive information system on transnational corporations could be developed. The *User's Guide* provides details of the information available from the system.

67. CTC is revising its publication *National Legislation relating to Transnational Corporations*, which was first published in 1978 and supplemented in 1980. The major areas under review are: main investment legislation and regulations; monitoring and screening investors; ownership, control and investment; foreign exchange control regulations; technology transfer and restrictive business practices; fiscal incentives and taxation; export processing zones; disclosure requirements under corporate laws; investment guarantees; governing law and dispute settlement. Approximately 40 countries, on a global basis, will be covered. It is expected that some 20 of these country profiles will be published in 1981.

68. Other areas of legislation which the CTC is presently covering include fiscal incentive laws and measures, tax haven laws and regulations, corporate disclosure requirements and regulations, divestment and local equity laws, and a special study on the laws and legislation of the People's Republic of China. The last study represents the first of the Centre's attempts to examine and assess in detail the countries whose legislation is covered in a generalized way in the publication on *National Legislation* referred to above. These studies are expected to be completed in early 1982.

69. On 1 May 1974, the General Assembly of OAS adopted resolution 167, according to which it was considered necessary for OAS to compile and make studies on the transnational enterprises operating in the countries of Latin America.

70. In addition, the Inter-American Juridical Committee, in its resolution 25, 8 March 1974, decided to maintain on the agenda the study of multinational commercial companies. Since then a number of reports on various aspects of the subject have been made to the

general secretariat of OAS with a request that they be distributed to all the Governments, organs, entities and groups of experts who are studying the question.

### V. TRANSFER OF TECHNOLOGY

#### A. *International code of conduct on transfer of technology*

71. In pursuance of resolution 89(IV) adopted by UNCTAD at its fourth session in May 1976 and by relevant General Assembly resolutions, a United Nations Conference on an International Code of Conduct on the Transfer of Technology was convened in October 1978. Since then, the Conference has held four sessions, the last one from 23 March to 10 April 1981.

72. The text of the draft Code (see TD/CODE TOT/25) presented to the fourth session consists of a preamble and 10 chapters. The chapters deal respectively with:

1. Definitions and scope of application;
2. Objectives and principles;
3. National regulation of transfer of technology transactions;
4. Restrictive practices;
5. Guarantees, responsibilities and obligations of parties;
6. Special treatment for developing countries;
7. International collaboration;
8. International institutional machinery;
9. Applicable law and settlement of disputes;
10. Other provisions.

73. The substantive provisions of the draft Code fall into two broad categories: first, those concerning the regulation of transfer of technology transactions and of the conduct of the parties to them, and secondly, those relating to steps to be taken by Governments to meet their commitments under the Code.

74. The first main category of provisions, establishing certain generally agreed and universally applicable standards, covers three areas: (a) determination of practices and arrangements involving transfer of technology which are to be deemed undesirable and under what conditions (chapter 4); (b) identification and clarification of responsibilities, obligations and rights of parties to transfer of technology transactions (chapter 5); and (c) the law and forum to be selected for the settlement of their disputes (chapter 9). The agreed provisions of the draft Code deal with areas (a) and (b) in a concrete

and fairly comprehensive manner. Together, these sets of provisions, which affect the terms on which technology is to be transferred, govern the transactions between parties and may be said to form the core of the regulatory part of the Code.

75. Provisions in the draft Code under the second main category—steps to be taken by Governments to meet their commitments to the Code—can be classified into the following three main types: (a) provisions related to the regulation of transfer of technology transactions by particular States. The draft Code provides indications or recommendations as to what measures States may take and sets forth certain general criteria that States should follow when enacting national legislation (chapter 3); (b) provisions concerning technology and related transactions that will be applied only where the acquiring country is a developing country. The aim of such measures is to facilitate and encourage the strengthening of the scientific and technological capabilities of these countries with a view to accelerating their development and to assist and co-operate with them in their efforts to fulfil their economic and social objectives (chapter 6); (c) provisions relating to international co-operative activities of States, on a bilateral, multilateral, regional or interregional basis, to facilitate the flow of technology and the growth of the technological capabilities of developing countries (chapter 7).

76. The draft Code envisages that the application and implementation of the Code are to be carried out at both the national and international levels. The appropriate steps to be taken at the national level include national policies, laws and regulations on the subject of transfer of technology (chapter 3). At the international level the Code will be implemented by the establishment and operation of an international institutional machinery within UNCTAD (chapter 8).

#### B. *Industrial property system*

77. At its third session, held from 17 to 28 November 1980, the Committee on Transfer of Technology adopted a resolution (14(III)) on the "Economic, commercial and development aspects of the industrial property system in the context of its on-going revision". In this resolution, the Committee requested the Secretary-General of UNCTAD to convene, in the first quarter of 1982, a group of governmental experts to continue to examine the economic, commercial and development aspects of industrial property in the transfer of technology to developing countries.

#### C. *Technology licence agreements: model law*

78. WIPO, with the assistance of a Working Group of experts selected in consultation with Governments,

prepared a chapter on technology licence agreements in a draft Model Law for Developing Countries on Inventions and Know-how. This chapter, together with certain other parts of the draft model law, was submitted for comments to the intergovernmental body of WIPO concerned (the WIPO Permanent Committee for Development Co-operation Related to Industrial Property) and was published in 1980.

#### D. *Publication*

79. WIPO published a guide entitled *Licensing Guide for Developing Countries*. The Guide deals with the legal aspects of the negotiation and preparation of industrial property licences and technology transfer agreements appropriate to the needs of developing countries. The Guide identifies the legal questions which may be detrimental to the interests of institutions and enterprises in developing countries, and suggests the solutions which are most likely to serve their interests.

80. The Guide has now been published in Arabic, English, French and Spanish. It has been widely distributed, particularly in developing countries. Its publication was the culmination of work in a WIPO Licensing Seminar, meetings of consultants and a Working Group on Guidelines for Industrial Property Licensing in Developing Countries. Altogether, 99 persons from 47 countries contributed to the work as participants in these meetings.

81. One of the topics of the Annual Report of the Inter-American Juridical Committee to the OAS General Assembly of 1980 concerned the "Legal aspects of co-operation in the field of transfer of technology". A resolution of the Committee pointed out some matters that should be considered to systematize an inter-American action for the transfer of technology on the basis of just and equitable principles.

82. For the purpose of arriving at the solution of these matters in its special area of its competence, the Inter-American Juridical Committee recommended:

Broad co-operation, within the scope of its specific competence, with other organs of OAS on legal aspects of transfer of technology. The said co-operation would take into account the results of the United Nations Conference on Science and Technology, the results of the United Nations Conference on an International Code of Conduct for the Transfer of Technology, and others

The development of a glossary of terms commonly used in transfer of technology agreements

Development of a study on essentially legal questions involved in the transfer of technology

The study, within the structure of OAS, of methodologies designed to put these recommendations into practice.



83. In order to co-operate with the studies of the Inter-American Juridical Committee on this matter, the general secretariat prepared a preliminary study on the "international transfer of technology and its juridical aspects".

## VI. INDUSTRIAL AND INTELLECTUAL PROPERTY LAW

### A. Work of WIPO

#### 1. Industrial property and patent information

##### (a) *Industrial property and patent information activities of particular interest to developing countries*

84. The objective is to be useful to developing countries in seven different respects:

Training specialists

Creating or modernizing domestic legislation

Creating or modernizing governmental institutions

Stimulating inventive activity

Stimulating transfer of technology

Creating a corps of practitioners

Exploiting technological information contained in patent documents.

Pursuant to the above objective WIPO has organized seminars, workshops and training courses in many countries.

##### (b) *Revision of the Paris Convention*

85. The objective is to revise the Paris Convention for the Protection of Industrial Property in order to introduce in it new provisions and to change certain existing provisions to better meet the needs of developing countries. The first session of the Diplomatic Conference on the Revision of the Paris Convention was held in Geneva from 4 February to 4 March 1980. Delegations from 89 countries participated; 14 intergovernmental organizations and 16 international non-governmental organizations were represented. The revision is still continuing.

##### (c) *Promotion of the acceptance of certain industrial property treaties*

86. The objective is to ensure that more countries become party to treaties dealing with the international protection of industrial property or certain international classifications (Paris Convention, Trademark Registration Treaty (TRT), Vienna Agreement (Figurative Elements of Marks), Budapest Treaty (Micro-organisms), Geneva Treaty (Scientific Discoveries), Strasbourg Agreement (IPC), Nice Agreement (Trademark Classifi-

cation) and Locarno Agreement (Industrial Designs Classification)).

##### (d) *Promotion of industrial property protection through new international arrangements*

87. The objective is to explore the need for an international treaty on the protection and/or international registration of computer software in order to institute international protection for software and/or to establish a reliable system for proving the origin and the date of creation of new software.

##### (e) *Promotion of industrial property protection outside treaties*

88. The objectives are to stimulate better contractual arrangements for the protection of inventions made within the framework of joint enterprises (mainly in East-West relations) and to stimulate new legislative and administrative measures which would enhance, through the judicious use of industrial property, the protection of consumers.

##### (f) *Promotion of the practical application of laws and treaties in the field of industrial property*

89. The objective is to draw a clear picture, region by region, of the present situation of industrial property law and institutions in the various countries. Surveys will cover the state of legislation, the organization and work of industrial property offices, the number and organization of practitioners, statistics on patents, trademarks etc.

##### (g) *Promotion of patent information and development of patent classification*

90. The objectives are to continue the improvement of the International Patent Classification, co-operation with INPADOC, and co-operation between patent offices in all aspects of patent documentation and patent information (standardization, modernization of reproduction and dissemination of patent documents etc.).

##### (h) *Development of trademark classification*

91. The objective is to continue the improvement of the Nice Classification of Goods and Services for the Purposes of the Registration of Marks, an important tool in the orderly registration of trademarks and service marks. "Improvement" means the covering of new products and services and the more precise description and classification of existing ones, in addition to the updating of the Classification in various languages.

##### (i) *Maintenance of general industrial property information services*

92. The objectives are: to allow, through forecasts based on statistical data, a better planning for industrial property activities in national offices, regional offices and the International Bureau; to inform promptly, by

means of a collection of industrial property laws constantly kept up to date, all those interested in the law of industrial property; to inform, by means of monthly periodicals, governments and interested private circles about the developments in the field of industrial property both on the national and the international levels; to facilitate, by means of a Guide to the Paris Convention, the application of the revised Convention; to inform, through the collection and dissemination of data concerning grants and registrations of industrial property titles, all those interested in the evolution and the trends of industrial property protection in countries in which the systematic publication of such data is lacking.

93. The industrial property statistics for the year 1978 were published in May 1980. The detailed tables of statistics for 1977 (publication "B") were published in January 1980.

94. The collection of laws and treaties on industrial property continued to be kept up to date; several such laws and treaties were published in the legislative series annexed to the review *Industrial Property*, which was published each month.

(j) *Co-operation with states and various institutions in matters concerning industrial property*

95. The objective is to ensure that, through regular contacts between the International Bureau on the one hand and the Governments and other international organizations on the other hand, there should be full awareness of what is being done and planned on either side, in order to inspire mutually more useful activities, to combine forces wherever possible and to avoid all unnecessary duplication.

2. *Copyright and neighbouring rights activities*

(a) *Copyright and neighbouring rights activities of particular interest to developing countries*

96. The objective is to be useful to developing countries in four different respects:

Training specialists

Creating or modernizing domestic legislation

Stimulating creative activity

Facilitating access to foreign works protected by copyright owned by foreigners.

(b) *Promotion of the acceptance of copyright and neighbouring rights treaties*

97. The objective is to ensure that more countries become party to the treaties dealing with the international protection of copyright and neighbouring rights.

(c) *Double taxation of copyright royalties*

98. An International Conference of States on the Double Taxation of Copyright Royalties remitted from

one country to another was held at Madrid from 26 November to 13 December 1979, convened jointly by WIPO and UNESCO. The delegates of 44 States participated, with observers from one intergovernmental and seven international non-governmental organizations.

99. The Conference established in Arabic, English, French, Russian and Spanish the text of a Multilateral Convention for the Avoidance of Double Taxation of Copyright Royalties, to which is attached an optional Model Bilateral Agreement on the subject. The texts are based on drafts prepared by a Committee of Governmental Experts at its third session in June 1978. The new Convention was deposited with the Secretary-General of the United Nations and remained open for signature until 31 October 1980.

(d) *Promotion of the practical application of laws and treaties in the fields of copyright and neighbouring rights*

100. The objectives include:

To draw a clear picture, region by region, of the present situation of copyright and neighbouring rights law and institutions in the various countries, such survey covering the state of legislation, the involvement of the government in the administration of such legislation, the role of authors' societies and other organized interest groups, statistics on works and their use etc.

To establish and disseminate a model statute for authors' societies

To study the relationship between copyright and computers

To expose, and study the practical remedies against, various forms of piracy of intellectual property

To study the best means of protecting works of folklore against abusive exploitation.

(e) *Maintenance of information services in the fields of copyright and neighbouring rights*

101. The objectives are to inform promptly, by means of collections and data bases constantly kept up to date, all those interested in copyright and neighbouring rights; to inform, by means of monthly periodicals, governments and interested private circles about the developments in the fields of copyright and neighbouring rights both on the national and the international levels; to facilitate, by means of the existing Guide to the Berne Convention, a Guide Copyright Glossary, a Guide to the Rome and Geneva Conventions, and various brochures, the understanding and the application of copyright laws and laws on neighbouring rights.

102. WIPO continued to keep up to date its collection of the texts of laws, regulations and treaties dealing with copyright and neighbouring rights.

103. The WIPO *Guide to the Berne Convention* was published in Portuguese in May 1980.

104. A *Copyright Law Survey*, containing summaries of national copyright laws, was published in French in February 1980 and in English in March 1980.

105. The WIPO *Glossary* of terms of law on copyright and neighbouring rights was published in three languages (English, French, Spanish) in March 1980. The Glossary contains 265 terms with their equivalents in the other languages, together with explanations.

(f) *Executive Committee of the Berne Union*

106. The Executive Committee of the Berne Union met in extraordinary session in October 1979. It held joint meetings with the Intergovernmental Copyright Committee set up under the Universal Copyright Convention.

107. The Committees discussed the question of the application of the Convention Relating to the Distribution of Programme-Carrying Signals Transmitted by Satellite (*Satellites Convention*) on the basis of the report of the Committee of Governmental Experts which met in Paris in June 1979 to draw up guiding principles for the implementation of the Satellites Convention by national legislators. These guiding principles consisted of two draft model provisions, one granting broadcasting organizations the right to authorize or prohibit the distribution of their programme-carrying signals (system of specific right) and the other prohibiting operations governed by the Convention (system of administrative and penal measures).

108. The Committees noted with approval the recommendations of the Working Group, which met in July 1979, to review all the problems posed for the developing countries by access to protected works, dealing with the application of the revised texts of 1971 of the Berne Convention and of the Universal Convention and with practical arrangements which would assist such application, including the recommendation that they should be kept regularly informed at their joint meetings of relevant projects, activities and achievements. It was also noted that the Directors General of UNESCO and WIPO were nearing conclusion of an agreement for the establishment of a joint international UNESCO/WIPO service for access by developing countries to works protected by copyright. This agreement came into operation on 1 January 1981. In pursuance of the recommendations of the above-mentioned Working Group with regard to the formulation of guiding principles, the respective secretariats of the Committees convened a meeting of a new Working Group in 1980. The results of their deliberations would be taken into account within the context of the joint international service.

109. The Committees noted the report of the Working Group which met in May 1979 in order to study the copyright problems arising from the use of computers for access to protected works or the creation of works. They took the view that, since the question was essentially an evolving one, it needed to be kept under active consideration. They noted in this respect that the secretariats would convene at the end of 1980 a Committee of Governmental Experts in order to analyse further the impact of computer storage and retrieval of works protected by copyright on their protection and the possible need for express recognition of copyright protection for works created with the help of computers, and to formulate tentative recommendations applicable at the national and international levels. The secretariats were asked to undertake studies on the question of copyright ownership when abstracts are prepared within documentation services, with regard to consequences for the relations between employers and employed or salaried authors. It was noted that the International Labour Office wished to be associated in this latter activity.

110. The Committees examined the report of their respective Subcommittees which met in July 1978 to examine the problems arising from the transmission by cable of television programmes.

111. Observing that certain of the problems were still in need of further study, they noted that independent experts would be called upon by the two Secretariats to meet at the beginning of 1980 in order to discuss the question of the impact of cable television in the sphere of copyright, particularly in respect of cinematography, and also to give their advice as regards the preparation of a worldwide forum in 1981 on combating the piracy of phonograms, films and other audiovisual recordings, a question which should be discussed more especially from the point of view of authors, producers of films, performers, producers of phonograms, broadcasting organizations and the general public.

112. The Committees endorsed the main lines of the recommendations adopted by their respective Subcommittees which met in September 1978 to examine the legal problems arising with regard to copyright as a result of the use of audiovisual cassettes and discs. Another meeting is expected in the future.

(g) *Co-operation with states and various institutions in matters concerning copyright and neighbouring rights*

113. The objective is to ensure that, through regular contacts between the International Bureau on the one hand and the governments and other international organizations on the other hand, there should be full awareness of what is being done and planned on either side, in order to inspire mutually more and more useful

activities, to combine forces wherever possible and to avoid all unnecessary duplication.

114. WIPO continued and strengthened its co-operation with UNESCO in the fields of copyright and neighbouring rights and with the ILO in the field of neighbouring rights. In particular, an agreement was concluded by WIPO and UNESCO on the establishment of a joint service to facilitate access to protected works.

### 3. *Registration activities in the field of industrial property*

#### (a) *Promotion of the acceptance of treaties*

115. The objective is to ensure that more countries become party to the Patent Co-operation Treaty, the Madrid Agreement Concerning the International Registration of Marks and the Hague Agreement Concerning the International Deposit of Industrial Designs.

116. Between 1 January and 14 September 1980 three countries (Democratic People's Republic of Korea, Finland, Hungary) deposited instruments of ratification or accession in respect of the PCT.

#### (b) *Registration activities*

117. The objective is to maintain registration and similar activities under the Paris Convention, the Patent Co-operation Treaty, the Madrid Agreement (Trademarks), the Hague Agreement (Industrial Designs) and the Lisbon Agreement (Appellations of Origin).

### B. *Work of CMEA*

118. In the framework of the Conference of Heads of Invention Agencies of CMEA Member Countries, draft agreements are being prepared for a single patenting document to safeguard innovations in CMEA member countries, and for possible legal protection for indications of origin and designation of place of origin of goods.

### C. *Work of EFTA*

#### 1. *Patents*

119. Some EFTA countries (Austria, Liechtenstein, Sweden and Switzerland) are members of the European Patent Organization (EPO) in Munich, together with a number of EC countries (Belgium, France, Germany, Federal Republic of, Italy, Luxembourg, the Netherlands and the United Kingdom). The aim of the EPO is to simplify the filing and granting, on the basis of unified provisions of substantive patent law, of patents valid within the Member States.

120. The EFTA countries above-mentioned also have the possibility of participating in the Community Patent Convention of 1975 which provides for the unitary effect of European patents for the EC countries and for which the preparatory work is still under way.

#### 2. *Trademarks*

121. Work is now being undertaken by an EFTA expert group to examine the possibility of harmonizing substantive trademark law in connection with related work presently carried out within the EC.

### D. *Work of OAS: the Inter-American Juridical Committee*

122. Since 1971, the matter of the revision of the Inter-American conventions on industrial property has been one of the most important topics of the Inter-American Juridical Committee.

123. The General Assembly of OAS, in its Resolution 51 of 1971, decided to convoke a meeting of governmental experts. The experts met at Washington, D.C. within the period from 26 June to 5 July 1973. A working group was established consisting of experts from Brazil, Chile, Guatemala, Mexico and the United States of America.

124. The Inter-American Juridical Committee, during its meeting held in the period July-August 1975, approved a report on the "Revision, Updating and Evaluation of Inter-American Conventions on Industrial Property", and resolved to convoke again a meeting of governmental experts on industrial property and the application of technology to development for the purpose of studying problems of industrial property and their relationship to the development of the countries of the inter-American system.

125. The General Assembly of OAS in its Resolution 234 of 1976, recommended that the Inter-American Juridical Committee prepare a draft convention (or draft conventions) for the revision and updating of the inter-American conventions on industrial property.

126. The Inter-American Juridical Committee at its meeting of July-August 1977, decided to prepare one or more draft conventions concerning patents of invention and industrial drawings and models. It was suggested that, in a latter phase, the Committee prepare a draft convention concerning commercial and industrial trademarks and commercial names.

127. In the meetings held from 9 January to 14 February 1978, the Inter-American Juridical Committee approved the report submitted by the working group formed by a decision of the Committee at its session of

11 August 1977. The conclusions of this report led the Committee to decide upon retaining the topic "Revision of Inter-American Conventions on Industrial Property", with special reference to "patents of invention and industrial drawings and models" as a priority topic for the next regular meeting of the Committee. The Inter-American Juridical Committee considered in its regular meeting from 30 July to 16 August 1979 the draft convention with 13 articles on industrial property.

128. The General Secretariat of the OAS has prepared a number of documents in support of this effort, the most recent of which was on industrial property and the revision of the Paris Convention of 1883 issued in July 1980. This study refers to the proposals suggested by the Ad Hoc Group of Experts of WIPO and the framework presented by the UNCTAD concerning the revision of the Paris Convention of 1883, in order to satisfy the goals of the less developed countries.

#### E. Work of ECE

129. The ECE Manual on licensing procedures contains 20 ECE country chapters describing national licensing legislation and policies, and provides legal and bibliographical references and relevant addresses. It also deals with the conditions for the transfer of technology and the rights and duties of licensor and licensee.

130. The Manual was adopted by the ECE Committee on the Development of Trade and the Senior Advisers to ECE Governments on Science and Technology (SC.TECH.AC.15/Rev.1). The Manual was adopted by the following ECE member countries: Belgium, Bulgaria, Canada, Czechoslovakia, Finland, France, German Democratic Republic, Germany, Federal Republic of, Hungary, Netherlands, Norway, Poland, Romania, Spain, Sweden, Switzerland, Turkey, United Kingdom and United States of America. The English version of the Manual was published in November 1980. The French version is expected to appear early in 1981 and the Russian version in late-1981.

### VII. INTERNATIONAL PAYMENTS

#### A. Documentary credits

##### 1. Revision of Uniform Customs and Practice for Documentary Credits (UCP)

131. The ICC Commission on Banking Technique and Practice is revising UCP. UCP are applied as standard terms to documentary credit operations

throughout the world. The project involves redrafting standard contract terms applied internationally to documentary credit operations.

132. The aim of the current work is to introduce modifications to bring the rules into line with the most current modern practices. In particular, documentary requirements are being re-examined in the light of developments in transport documentation and techniques, and consideration is being given to the desirability of introducing provisions relating to stand-by letters of credit in response to a suggestion by UNCITRAL.

##### 2. Standard application form for documentary credits

133. The ICC Commission on Banking Technique and Practice is preparing a standard application form to be used by applicants for documentary credits. The form will include all details required by the bank called on to issue the credit. It will facilitate applications by introducing a standard format (based so far as possible on the ECE layout key) in harmony with the forms already used by banks when issuing documentary credits subject to Uniform Customs and Practice for Documentary Credits. An accompanying explanatory brochure on use of the form is also being prepared. The information provided in the form is incorporated in the documentary credit subsequently issued by the recipient bank.

#### B. Rules for foreign exchange contracts

134. The ICC Commission on Banking Technique and Practice in collaboration with representatives of the "Group of Ten" banks in drafting rules governing forward foreign exchange contracts. The rules deal with the formalities on conclusion of a foreign exchange contract, and the consequences between the parties when the contract cannot be carried out.

135. The objective of the above rules is to establish internationally accepted standards applicable to the liquidation of such contracts in cases when one of the parties is unable to perform its contractual obligations. It is intended that these rules be adopted by banks as contractual terms in their foreign exchange contracts.

#### C. Negotiable instruments

136. At its fourteenth session in October 1980, the Hague Conference on Private International Law decided to take under consideration the preparation of a convention on the law applicable to negotiable instruments as a subject to be included in the agenda of a future session.

[A/CN.9/202/Add.2\*]

## VIII. INTERNATIONAL TRANSPORT

## A. Transport by sea and related issues

## 1. International shipping legislation

1. The UNCTAD Working Group on International Shipping Legislation was established by resolution 7 (III) of the Committee on Shipping pursuant to Conference resolution 14 (II) and resolution 46 (VII) of the Trade and Development Board. Under its terms of reference the Working Group is to review the economic and commercial aspects of international legislation and practices in the field of shipping from the standpoint of their conformity with the needs of economic development, in particular in the developing countries, in order to identify areas where modifications are needed and in the light of such a review, to make recommendations which would serve as a basis for further work in this field.

2. During 1980, the ESCAP secretariat initiated a project aimed at updating and improving existing maritime legislation in ESCAP member countries. Assistance is provided by the Netherlands Government in undertaking a survey in a number of countries. The results of the survey will constitute the basis for further regional discussions on the subject.

## 2. Charter-parties

3. The subject of charter-parties is part of the work programme adopted by the UNCTAD Working Group on International Shipping Legislation at its first session in 1969. The Working Group, at its fourth session held from 27 January to 7 February 1975, considered a report prepared by the UNCTAD secretariat entitled "Charter Parties" (TD/B/C.4/ISL/13). This report examines the principal clauses in voyage and time charter-parties and suggests, *inter alia*, that such clauses be standardized and that the introduction of mandatory international legislation on certain aspects of the liability of the shipowners and charterer be considered.

4. Having considered this report, the Working Group requested the UNCTAD secretariat to carry out additional studies, which are now in progress in the UNCTAD secretariat, involving a comparative analysis of the principal clauses in voyage and time charter-parties. On the basis of these studies the UNCTAD secretariat will submit additional data to the Working Group that should help it to determine which of the main clauses in voyage and time charter-parties are capable of standardization, harmonization and improvement and to

select areas in chartering activities that may be suitable for international legislative action. The Working Group will consider the new studies and decide on future action on the subject of charter-parties.

## 3. Marine insurance contracts

5. Legal problems in marine insurance form part of the work programme of the Working Group. The UNCTAD secretariat issued a report entitled "Legal and Documentary Aspects of the Marine Insurance Contract" (TD/B/C.4/ISL.27 and Corr.1 and Add.1) which was submitted to the sixth session of the Working Group, which met from 18 to 26 June 1979. The report analysed various legal and documentary aspects of national marine hull and cargo insurance contract forms, identifying problems caused by ambiguities, inequities or lacunae in commonly used national policy forms, and recommended the establishment of an international legal basis for marine insurance contracts to be developed by an internationally representative group of marine insurance experts (including representatives of insurers and assureds). After consideration of the report, the Working Group unanimously adopted resolution 3 (VI) recommending the establishment of a subgroup of experts at the seventh session of the Working Group to (i) examine the existing marine insurance policy conditions and practices used in national markets covering international business, (ii) investigate the different legal systems governing marine insurance contracts, and (iii) in the light of these studies and bearing in mind the suggestions contained in the UNCTAD secretariat report, draw up a set of standard clauses as a non-mandatory international model.

6. For the seventh session of the Working Group, the secretariat prepared two studies entitled the "Legal and documentary aspects of the French marine insurance legal regime" (TD/B/C.4/ISL/30) and the "Legal and documentary aspects of Latin American marine insurance legal regimes" (TD/B/C.4/ISL/31), which analysed basic aspects of the marine insurance legal regimes in the countries concerned. The secretariat also prepared an "Informal Working Paper to assist in the drawing up of a set of standard clauses (hull)" (TD/B/C.4/ISL/L.53 and Corr.1), which presented some considerations that the Working Group might wish to bear in mind in organizing its work, and also submitted various draft clauses on selected aspects of the marine hull insurance contractual relationship. As a result of decision 39 (IX), adopted at the ninth session of the Committee on Shipping, the seventh session of the Group dealt with hull insurance.

7. The seventh session of the Working Group, using the Informal Working Paper prepared by the secretariat as a basis for its work, drew up composite texts on a set of risks clauses and on a collision liability clause. At the end of its session the Group decided to continue its work

\* 20 May 1981.

on hull insurance for part of its next session, and to commence work on cargo insurance.

8. The ICC's Commission on Insurance Problems has followed UNCTAD's project on clauses of insurance contracts. In a statement, adopted by the ICC Council in November 1980, the ICC Commission stressed that action aimed at producing standard clauses which could be used as a non-mandatory model should be supported, if such clauses will assist developing markets to produce their own clauses in a clear and concise form. However the ICC Commission doubted that standard clauses are really necessary insofar as Marine Cargo and Hull Policies are concerned, since those clauses are already well-known and have been the subject of legal interpretation over so many years.

9. The ICC Commission which regroups users as well as insurers underscored that any standard clauses should remain non-mandatory, since the flexibility at present offered to consumers to select the policy conditions which are best suited to their needs and also to choose which markets to use for the placement of their insurance should not be jeopardized.

10. The ICC Commission emphasizes the need to develop sufficient training and education in the field of marine insurance contracts. As a legal document, the insurance policy cannot be phrased in over-simplified language, because it must as far as possible take into account all those aspects of international transit which could affect the insurance. It is therefore of utmost importance that those engaged in commerce should be conversant with other documents relating to trade, such as contracts of sale, bills of lading etc. With this in mind the Commission decided by the end of 1980 to propose that marine insurance problems should be introduced in training seminars to be held in third-world countries in 1981 and 1982.

#### 4. Open registry shipping

11. This subject has been kept under continuous review by the UNCTAD Committee on Shipping since an *Ad Hoc* Intergovernmental Working Group (on the Economic Consequences of the Existence or Lack of a Genuine Link between Vessel and Flag of Registry) on the subject met in February 1978 and concluded, *inter alia*, that the expansion of open registry (i.e. flag of convenience) fleets had adversely affected the development and competitiveness of the merchant fleets of developing countries. The secretariat prepared various studies on relevant legal issues for consideration by the fifth session of UNCTAD (Manila, May 1979), the Committee and the *Ad Hoc* Group. These studies suggested elements which could advisedly be included in the definition of a "genuine link" between a vessel and its country of registry.

12. At its ninth session in September 1980, the Committee on Shipping adopted a resolution 41 (IX) which requested studies on social/economic consequences, accountability of owners, safety and social conditions and fiscal regimes of the open registry fleets. The Trade and Development Board has convened a Special Session of the Shipping Committee in May 1981 to consider the subject further on the basis of the additional studies.

#### 5. Implementation of the Convention on a Code of Conduct for Liner Conferences

13. On 6 April 1974 the United Nations Conference of Plenipotentiaries on a Code of Conduct for Liner Conferences, by a vote of 72 to 7 with 5 abstentions, adopted the Convention on a Code of Conduct for Liner Conferences (for the text of the Convention, see TD/CONF/13/Add.1).

14. The status of the Convention was considered at the fifth session of the United Nations Conference on Trade and Development (Manila, 6 May-1 June 1979). The representatives of a number of developed countries announced the intention of their Governments of becoming Contracting Parties to the Convention. It may therefore be expected that the Convention will enter into force at an early date. The Conference adopted without dissent resolution 106 (V), which, *inter alia*, calls upon Contracting Parties to the Convention to take all necessary measures towards the early implementation of the Convention; invites States which are not yet Contracting Parties to the Convention to consider becoming Contracting Parties, and in doing so, to give full consideration to the interests of the developing countries in the Convention; and requests the Secretary-General of UNCTAD to give guidance and assistance, on request, to the Governments of developing countries in putting the Code into effect. Such guidance is being provided by the secretariat.

15. The UNCTAD secretariat, on the basis of information provided by the Office of Legal Affairs of the United Nations, provides on a regular basis to member States of UNCTAD information on signatures, ratifications, acceptances, approvals of or accessions to the Convention. The UNCTAD secretariat has also offered its services, if requested, to assist and guide States in ratifying or acceding to the Convention. By 31 December 1980, 51 countries had become Contracting Parties to the Convention.

#### 6. Model rules for regional associations and joint ventures in the field of maritime transport

16. The UNCTAD secretariat is preparing model rules on regional associations (ports, shippers, ship-owners) and joint ventures in the field of maritime transport. The model rules, which may later be published as a handbook, is intended to assist co-operation among



developing countries in the field of shipping and ports. This activity has arisen as a result of increasing demands for such rules, which have surfaced during technical assistance projects.

#### 7. *Treatment of foreign merchant vessels in ports*

17. The UNCTAD Committee on Shipping, at its seventh session held in November 1975, considered a report prepared by the UNCTAD secretariat entitled "Treatment of foreign merchant vessels in ports" (TD/B/C.4/136). The report reviews the international rules and regulations having a bearing on the status of foreign merchant vessels in ports and examines the Conventions and Statutes on the International Regime of Maritime Ports of 1923. The Committee has requested the secretariat to monitor international developments in this field, and in the light of this information, it will decide at a later date whether further work on this subject is necessary.

#### 8. *Freight forwarding*

18. The UNCTAD secretariat has circulated a report examining freight forwarding operations and services, including applicable legal regimes, in particular as they relate to the strengthening of freight forwarding in developing countries (document UNCTAD/SHIP/193).

#### 9. *"Baltim-Konstantsa-78"*

19. The "Baltim-Konstantsa-78" charter was adopted by the Conference of Freight and Shipping Organizations of CMEA Member Countries in 1980; the text of the stipulation concerning the inclusion of the "Basic conditions for the possible allocation of tonnage and freight to shipping undertakings in CMEA member countries" is included in the *pro formas* of the charters which are agreed between shipping undertakings in the CMEA members countries.

#### 10. *Maritime fraud*

20. At its eleventh regular session the IMCO Assembly requested the Council to provide for a study of "the question of barratry, the unlawful seizure of ships and their cargoes and other forms of maritime fraud with a view to making recommendations as to the action which IMCO should take in the matter". Pursuant to the request of the Assembly, the Council decided to establish an *Ad Hoc* Working Group on Barratry, the Unlawful Seizure of Ships and their Cargoes and other forms of Maritime Fraud.

21. The above Working Group is to consider the subject and report to the Council on:

"(a) The nature and prevalence of such acts which threaten the international community;

"(b) Legal, administrative and other actions being taken by States, international organizations and other interests concerned to deal with these threats;"

22. The Group is to make recommendations to the Council as to the action IMCO should take in this matter. The Group met in Paris on 24 and 25 November 1980. The Working Group has recommended a resolution on the subject which will be considered by the Council in June 1981 and eventually by the Assembly in November 1981.

23. ICC is preparing a Guide on the Prevention of Maritime Fraud.

#### 11. *Carriage of noxious and hazardous substances by sea: draft convention on liability and compensation*

24. The Legal Committee of IMCO continued its work on the preparation of a draft convention on liability and compensation in connexion with the carriage of noxious and hazardous substances by sea. It is expected that the draft will be submitted to a diplomatic conference in 1982.

#### 12. *"AMOCO CADIZ" disaster: legal questions*

25. This is one of the two subjects assigned high priority on the work programme of the Legal Committee of IMCO. The Committee has currently before it proposals which envisaged the possibility of draft provisions being prepared on some aspects of the subject for consideration at the diplomatic conference planned to be held in 1982.

26. The particular aspects to which special reference has been made in this connexion include:

Draft Protocol to the 1969 Intervention Convention in respect of Reporting

Possible Review of the Limits laid down in the 1969 Civil Liability Convention and the 1971 Fund Convention.

#### 13. *Convention on Civil Liability for Oil Pollution Damage*

27. The Legal Committee of IMCO has already prepared a set of draft articles for a protocol to extend the 1969 Civil Liability Convention to oils not covered by that Convention. The Committee gave further consideration to the draft articles of the proposed protocol at its forty-fourth session in November 1980. Further consideration is expected to be given to the draft articles in the near future, and there is the possibility that the draft articles finally approved by the Legal Committee will be submitted for consideration and adoption by the diplomatic conference scheduled to be held in 1982. It is, therefore, to be assumed that some work on this subject will be undertaken by the Legal Committee at least during the first half of 1982.

#### 14. *Civil liability for damage caused by small craft*

28. The ICC Inland Transport Committee is considering the elaboration of a draft convention on civil liability for damage caused by small craft. Work is to start in 1981. It is to be noted that UNIDROIT has prepared such a draft convention (TRANS/SC.3/GE.33/R.5).

#### 15. *Maritime liens and mortgages*

29. One of the subjects included in the work programme of the IMCO legal Committee for 1982/1983 is "possible review of the CMI Brussels Conventions with a view to their being replaced by up-dated conventions under the auspices of IMCO". One of the Brussels conventions specifically referred to in this connexion is the 1926 Convention for the Unification of Certain Rules Relating to Maritime Liens and Mortgages, and the 1967 revision thereof.

#### 16. *General average*

30. The UNCTAD secretariat, as part of the Work Programme of the Working Group on International Shipping Legislation, will shortly be taking up the study of general average, and other subjects in the maritime field pursuant to UNCTAD resolution 14 (II).

#### 17. *Seminars*

31. The UNCTAD secretariat has organized seminars for participants from developing countries on Ocean Chartering and on Ocean Transport Documentation, dealing with both legal and commercial aspects of these subjects. It expects to hold further seminars on legal aspects of other maritime topics in the future.

#### 18. *Technical assistance*

32. As part of its ongoing work, substantive support is provided by UNCTAD to legal elements in various technical co-operation projects, in particular on maritime legislation in Central America and West Africa.

#### 19. *Carriage of goods by inland waterway*

33. UNIDROIT is preparing a Convention on contract for the carriage of goods by inland waterway. Following initial work by UNIDROIT, ECE sought to implement a Convention aimed at filling the gap in international transport law deriving from the absence of uniform rules governing contracts for the carriage of goods by inland waterway. Efforts to this end resulted in failure in 1960 and, after an offer by UNIDROIT to revise the draft, three sessions of a Committee of Governmental Experts convened by the Institute and chaired by Professor R. Herber (Federal Republic of Germany) were held between 1973 and 1975. At the third session, the Committee completed a first reading of the

revised preliminary draft, and a compilation by Professor R. Loewe (Austria), Rapporteur to the Committee, of the texts prepared by the Committee during its first three sessions was then sent to Governments and to interested organizations for their observations so that, after their consultation, a decision might be taken on whether there would be a fourth session for a second and last reading of the preliminary draft which could then be sent to the ECE in accordance with the mandate conferred on UNIDROIT by the latter.

34. The replies of States indicated that the fundamental difference of opinion existing among the Rhine States on the exoneration of the carrier for fault in the navigation of the vessel still subsisted. In view of the deadlock on this point, the Governing Council, at its fifty-fifth session (September 1976), instructed the Secretariat to transmit to the ECE a note outlining the work of the Committee of Experts to date and informing it of the Council's decision temporarily to suspend work on the elaboration of the draft CMN, on the understanding that the UNIDROIT Committee might be convened for a fourth meeting if a change in the attitudes of States were to justify the taking of such a step.

35. Following communications from the President of the Central Commission for the Navigation of the Rhine and of the Chairman of the UNIDROIT Committee of Governmental Experts recommending that the work of the Committee be resumed, as well as a request to the same effect from the ECE, the Governing Council decided at its fifty-ninth session, held in May 1980, that a fourth meeting of the UNIDROIT Committee of Governmental Experts should be convened in 1981.

36. It is to be anticipated that further work on the draft CMN Convention will be directed on the one hand to overcoming the difficulty regarding the exoneration of the carrier for liability for damage caused by fault in the navigation of the vessel and on the other to a general updating of its provisions, taking account of recent developments and in particular of the changes introduced into maritime law by the Hamburg Rules in the carriage of goods by sea.

#### B. *Transport over land and related issues*

##### 1. *Civil liability for damage caused by hazardous cargoes*

37. The Secretariat of UNIDROIT is preparing a draft Convention relating to liability and compensation for damage caused during the carriage by land of hazardous substances. Increasing concern at the risks caused by the carriage in bulk of hazardous substances over land as witnessed by the tragic accident at Los Alfaquès in Spain in July 1978, led the Governing Council to request the secretariat to undertake a

preliminary report on the feasibility of preparing an international Convention relating to liability and compensation for damage caused during the carriage over land of hazardous substances, which might serve as a parallel to the draft Convention concerning liability for the damage caused by such substances when carried by sea, on which work has reached an advanced stage in the Inter-governmental Maritime Consultative Organization (IMCO).

38. The secretariat prepared the report and, in its conclusions, it set out a number of tentative considerations which it believed could assist those who might be called upon to elaborate a Convention in this field. These considerations are:

The principal aim of the prospective Convention must be to ensure adequate compensation for victims

Such compensation must not be a theoretical possibility but a practical reality

There must be a guarantee that compensation will be paid, which almost certainly presupposes a system of compulsory insurance or alternative security

Any system of compulsory insurance must be devised with the following factors in mind:

(a) Available market capacity, which may in the first instance call for a restriction of the prospective Convention to ultra-hazardous substances capable of causing massive or catastrophic damage;

(b) The financial capability of the insured to meet the obligation to take out insurance;

(c) The extent to which premiums will be affected by the determination of the person who is to be required to obtain insurance cover (i.e. the carrier, owner of the vehicle or vessel concerned, shipper, producer etc.);

(d) Possibility of supervision of the system (perhaps by granting licences for the carriage of hazardous substances);

(e) Availability to the victim of a direct action against the insurer:

The combination of factors relating to insurance will be preponderant in determining the person or persons to be held liable under the prospective Convention by a process of channelling which should cut down the possibility of recourse actions to a minimum

The imposition of a system of compulsory insurance will almost certainly call for a limitation on the compensation payable by the person or persons to be held liable, although the possibility should not be overlooked of creating a supplementary fund to be financed by the commercial interests involved or by States

In the interest of victims the defences open to the person or persons liable should be extremely limited

The prospective Convention should make the most effective provision for recovery by the victim through the introduction of rules relating to jurisdiction and enforcement of judgements

While practical considerations will probably call for some restriction on the number of substances to be covered by the instrument, its geographical scope should be as wide as possible and in particular all efforts should be made to avoid instituting a regime, based on the fact that the carriage was international, alongside existing national regimes

The prospective Convention should apply the same rules to carriage by road, rail, inland waterway (and possibly pipelines), the only justification for departures from the principle being based on the risk of unification introducing distortions in competition between the different modes of transport and on technical considerations relating to differences in the manner and volume of the carriage of certain substances.

39. The Secretariat study was submitted to the Governing Council at its fifty-ninth session and a decision was taken to convene a Committee of Governmental Experts which would meet in 1981 to consider the feasibility of preparing uniform rules in this connexion. The first session of the Committee took place from 16 to 20 March 1981.

## 2. *Harmonization of frontier control of goods*

40. The ECE Inland Transport Committee is undertaking a project involving the elaboration of a draft international convention on harmonization of frontier controls of goods. The convention would aim at reducing the requirements for completing formalities as well as the number and duration of customs and other frontier controls of goods (medico-sanitary, veterinary, phytosanitary and quality controls; public safety controls; controls of compliance with technical standards).

41. The legal issues involved in the project concern, *inter alia*, the co-ordination of controls, resources of the control services, international co-operation, documentation and exchange of information.

42. The following international organizations have participated in the work on this project: CCC, EEC, EPPO, FAO, IMCO, INTERPOL, IOE, IRU, ISO, OECD, UIC, UNCTAD, WHO. A final text has not yet been adopted.

## 3. *Customs transit*

43. The ECE Inland Transport Committee is undertaking a project involving consideration of the possibility of establishing a link between the different existing systems of customs transit. The legal issues involved in the project concern, *inter alia*, mutual recognition of the

validity of the information contained in the transit documents, acceptance of seals, and administrative co-operation. No decision has yet been made as to the establishment of a link between customs transit systems and the form (resolution or convention) that an eventual link would take.

44. The following international organizations are participating in the work on this project: the Customs Co-operation Council (CCC), the European Economic Community (EEC) and the International Road Transport Union (IRU). CCC, having undertaken similar work in the past, resumed consideration of this question in parallel with the work in the ECE; it has however decided to suspend further consideration pending the results of the deliberations within the ECE.

### C. *Transport by air*

45. The general work programme of the Legal Committee of ICAO includes the following:

Legal status of the aircraft commander

Liability of air traffic control agencies

Aerial collisions

Consideration of the Report of the Subcommittee on the problem of liability for damage caused by noise and sonic boom

Study of the status of the instruments of the "Warsaw System"

Study of a possible consolidation of international rules contained in the Convention on Damage Caused by Foreign Aircraft to Third Parties on the Surface (Rome 1952), the Draft Convention on Aerial Collisions and the subject of Liability of Air Traffic Control Agencies

Lease, Charter and Interchange of Aircraft in International Operations (Resolution 8 of the Guadalajara Conference)—Problems with respect to the Tokyo Convention.

### D. *Liability of international terminal operators*

46. UNIDROIT is undertaking the preparation of uniform rules on the liability of persons, other than the carrier and the forwarding agent, who has been given custody of goods during or after international transport operations. In the course of two meetings, held in April 1978 and January 1979, a Study Group chaired by Professor K. Grönfors (Sweden) and composed of members from France, the German Democratic Republic, Germany, Federal Republic of, India and the United Kingdom, worked out a preliminary draft Convention on the liability of international terminal operators.

47. In embarking on the preparation of uniform rules relating to warehousing operations, the Group recognized the complexity of the problems involved. Not only was there the distinction between long-term and transit warehousing but in addition customs and practices differed widely between one warehouseman or terminal operator and another, not only as regards the conduct of their operations but also in respect of the liability regime applied. Unlike carriage operations, warehousing is a sphere of activity which has been left almost exclusively within the province of national regulations.

48. However, there was a general feeling that there was a real need for the introduction of uniform rules on the warehousing contract especially in the context of the international carriage of goods. This latter subject has, to a very large extent, been regulated by international conventions and yet, the most frequent cases of damage to, or loss of, goods could be proved statistically to occur before and after transport operations. In these circumstances it seemed important to try to fill in the gaps in the liability regime left by the existing international transport law conventions and to ensure the availability of a recourse action to the carrier or the multimodal transport operator against non-carrying intermediaries such as the warehouseman or terminal operator, an objective which in the opinion of some members of the Group could only be achieved by insisting upon the issuance of a document acknowledging receipt of the goods. This document, it was further suggested, might be of importance in the facilitation of international trade if it were to be of a negotiable character.

49. Given these premises, the majority of the Group was of the opinion that it would be desirable to limit the application of the future instrument to international warehousing operations as it was felt that unification of domestic law, where there are substantial differences in conceptual approach between different legal systems, might be an unrealistic goal at the present time. A consequence of this conclusion was a decision to deal only with those warehousing operations which are linked to the international carriage of goods as it is this dynamic element alone which would permit the delimitation of the scope of the draft Convention in such a way as to exclude from its application purely domestic warehousing operations. It was further agreed that the future instrument should be applicable irrespective of the mode, or modes, of transport preceding or following the warehousing operations.

50. The regulation of international warehousing operations is, therefore, the main objective of the draft Convention but the Group recognized at the same time that modern terminal operators often undertake a number of services associated with the handling of goods, such as loading, stowage and unloading and while there was little support for the idea of extending the

scope of the instrument to cover the performance of such operations in all cases, and thus to regulate what might be termed the "*contrat de transit*", it was nevertheless agreed that to the extent that the operator who undertakes the safekeeping of goods also undertakes to perform or to procure the performance of such operations, he should be liable in the same way and on the same basis as he would be in the performance of his obligation to ensure the safekeeping of the goods.

51. Another question which was the subject of discussion by the Group was that of the character of the future instrument. While some members argued in favour of a Convention of a traditional nature, the provisions of which would be of a mandatory character, others considered that it might be difficult to overcome the pressure of the professional interests involved on States not to adopt such a Convention and in consequence a compromise solution was reached. Those States which wished to do so might apply the provisions of the future instrument to all terminals operating on their territory while others should be free in accordance with article 17, to make a declaration to the effect that they would only guarantee their application to authorized international terminal operators who would be designated as such on condition that they voluntarily undertake to observe the minimum rules laid down in the Convention. Those pleading in favour of this latter solution considered that such voluntary acceptance of the minimum rules might be obtained if the Convention were to contain a number of incentives such as a moderate liability regime, based on that of the Hamburg Rules, a limitation on liability which could be broken only in highly exceptional circumstances, the granting of a general lien over the goods and above all the fact that the insertion of those rules in general conditions would be recognized by the courts of Contracting States whereas otherwise such conditions would be exposed to the risk of being struck down in the face of the growing pressure of consumer protection lobbies.

52. As regards the general structure of the draft Convention prepared by the Study Group, it may be stated that it is built around the concept of the "international terminal operator (ITO)", who is defined in article 1 as "any person who undertakes [against payment] the safekeeping of goods before, during or after international carriage, either by agreement or by actually taking in charge such goods from a shipper, carrier, forwarder or any other person with a view to their being handed over to any person entitled to take delivery of them". As mentioned above, the draft is thus concerned with warehousing operations connected with international carriage which, for the purposes of the draft Convention, means "any carriage in which, according to the contract of carriage, the place of departure and the place of destination are situated in two different States".

53. Article 2 of the draft lays down the general statement of the liability of the ITO in respect of the performance of his obligations for the safekeeping of the goods and also indicates the period during which he shall be liable. The article further affirms the liability of the ITO in respect of certain services connected with the handling of the goods which he performs, or the performance of which he procures, in addition to the safekeeping of the goods.

54. Two key articles of the draft are articles 3 and 4. Article 3 is concerned with the issuance by the ITO of a dated document acknowledging receipt of the goods and stating the date on which they were actually taken in charge. Such a document, however, need only be issued if requested by the customer. Article 4, which is closely modelled on a corresponding provision in the UNIDROIT draft Convention on the hotelkeeper's contract, deals with the ITO's rights of retention and sale over goods.

55. Articles 5 to 14 of the draft Convention are based to a very large extent on the corresponding provisions of the Hamburg Rules and this is true especially of the basic liability regime (presumed fault with the burden of proof reversed) and the rules governing limitation of liability, availability of defences, loss of the right to limit liability, notice of loss, prescription, nullity of stipulations contrary to the provisions of the Convention and unit of account. In particular, article 13 provides that the Convention "does not modify the rights or duties of a carrier which may arise under any international Convention relating to the international carriage of goods".

56. Articles 15 to 22 contain a set of draft final clauses and, like the draft preamble, these were not discussed at any length by the Group. The one exception is article 17 which makes provision for a declaration by States excluding the absolute mandatory character of the future instrument, which has been mentioned above in paragraph 15 of this report and which is discussed in detail below in paragraph 86 *et seq.*

57. The Group realized that the draft Convention prepared by it did not deal with a number of important aspects of warehousing contracts. In particular it was silent on the question of the customer's obligations such as those of paying the price for the services and, in the event of his tendering dangerous goods to the ITO for handling or safekeeping, that of giving the necessary instructions. Neither did it deal with the ITO's right to dispose of or sell dangerous goods nor with the obligations of the customer to tender the goods for safekeeping or the ITO to take them in charge when a contract for their safekeeping had been concluded in advance. It was, in effect, an outline draft concerned essentially with establishing a set of minimum rules governing the liability of ITOs and many points of detail have been omitted which might be fitted in at a later stage or alternatively regulated by standard conditions

which, if a need for them were to be recognized, might be prepared by the interested commercial Organizations such as the ICC, the CMI and IAPH. It was noted that other organizations might wish to co-operate in this task but what was above all to be avoided was incompatibility between such conditions and the future Convention on the liability of international terminal operators.

58. In accordance with a decision of the Governing Council of UNIDROIT, the text of the preliminary draft Convention was circulated to Governments and to the interested international organizations for observations. An analysis of these comments will be submitted first to the Governing Council, and then to the Study Group, with a view to a reconsideration of the present text of the draft. These observations are not yet complete but one recurring theme which has been noted by the Secretariat of UNIDROIT so far is a call for adequate regard to be had to the new United Nations Convention on Multimodal Transport.

#### E. Multimodal transport

59. On 24 May 1980, the United Nations Conference on International Multimodal Transport, convened under the auspices of UNCTAD, adopted by consensus of the 83 participating countries the United Nations Convention on International Multimodal Transport of Goods, marking a successful conclusion to more than seven years of negotiations (for the text of the Final Act and the Convention, see TD/MT/CONF/15 and 16).

60. The new Convention is open for signature in New York from 1 September 1980 until 30 August 1981, and can be acceded to thereafter. The Convention will enter into force 12 months after 30 States become Contracting Parties.

61. The UNCTAD secretariat would, as in the case of the Liner Code, respond to requests from developing countries to assist them in implementing the Convention, and is assisting these countries in regard to various legal aspects of multimodal transport and its regulations. Additionally, pursuant to resolution 36(IX) adopted at the ninth session of the Committee on Shipping in September 1980, the secretariat will prepare reports on legal issues as to designated aspects of multimodal transport.

#### F. International agreement on container standards

62. Pursuant to decision 6(LVI) of the Economic and Social Council and decision 118(XIV) of the Trade and Development Board, the *Ad Hoc* Intergovernmental Group on Container Standards was established within UNCTAD with terms of reference which included the examination of the practicability and desirability of

drawing up an international agreement on container standards. The *Ad Hoc* Intergovernmental Group considered this question at its first and second sessions, which were held from 1 to 12 November 1976 and from 20 November to 1 December 1978, respectively.

63. Having considered the reports (TD/B/AC.20/6 and TD/B/AC.20/10) of the *Ad Hoc* Intergovernmental Group and the proposals contained therein, the Trade and Development Board decided in March 1980 to remit to the Committee on Shipping the question of container standards for regular review as well as the decision of drawing up an international agreement on container standards at an appropriate future date.

### IX. INTERNATIONAL ARBITRATION

#### A. Activities concerning specialized types of arbitration

##### 1. Arbitration in the field of international contracts of building construction

64. An *ad hoc* Working Party on arbitration and building construction, set up in 1981, by the ICC Commission on International Arbitration is preparing a Guide on the settlement of disputes in building construction contracts.

65. The disputes arising in this field appear to be complex owing to technicalities, ever-increasing costs in individual building projects, performance of the contract spread over a specific period and the lapse of time between the signature of the contract, the appearance of the technical difficulties and the appointment of the arbitrators.

66. The project is undertaken in collaboration with representatives of a number of institutions such as the International Bar Association (IBA), the German Institute for Arbitration and the International Working Group on FIDIC Civil set up by the Institute of German and International Construction Law. The target date for completion is the end of 1982.

##### 2. Arbitration and competition law

67. In 1978 the *ad hoc* "Arbitration and Competition Law" Working Party, set up by the ICC Commission on International Arbitration, initiated a study aimed at developing arbitration in accordance with economic policies designed to ensure free competition. The arbitrariness of disputes involving anti-trust law in national and community laws were analysed and certain recommendations were made. This project should be completed by the end of 1981.

### 3. *Arbitration and related contracts*

68. An *ad hoc* Working Party, set up in 1978 by the ICC Commission on International Arbitration, is studying the desirability and practicability of guaranteeing unity of arbitral proceedings in cases where performance of the principal contract is dependent on or inseparable from elements provided by third parties as in "turn-key" contracts.

### 4. *Interlocutory arbitration*

69. An *ad hoc* Working Party on interlocutory arbitration, set up in 1981 by the ICC Commission on International Arbitration, is undertaking the preparation of a system of interlocutory arbitration which would enable the parties to obtain the immediate nomination of an arbitrator to enable this arbitrator to take interim or provisional and possibly conservatory measures pending a substantive arbitration.

70. The course of action contemplated is guide and/or model contractual clauses. The date of completion is expected to be some time in June 1982.

### 5. *Disputes arising from economic, scientific and technical co-operation*

71. With a view to improving ways and means of settling questions which arise among the economic organizations of CMEA member countries, a Convention on Settlement by Arbitration of Civil Law Disputes Arising from Economic, Scientific and Technical Co-operation was drawn up and signed on 26 May 1972. Parties to the Convention are Bulgaria, Cuba, Czechoslovakia, German Democratic Republic, Hungary, Mongolia, Poland, Romania and the Soviet Union. The Convention has been registered with the United Nations Secretariat. Uniform Rules for Arbitration Tribunals attached to the Chambers of Commerce of CMEA member countries have also been drawn up. The Uniform Rules were drafted by the CMEA Conference on Legal Matters and approved by the CMEA Executive Committee in 1974.

72. In the programme of work of the CMEA Conference on Legal Matters provision has been made for a study of the practical implementation of the Convention and Uniform Rules referred to above with a view to the possible improvement of these documents and/or their application in practice.

### B. *Furtherance of arbitration on the regional level*

73. In February 1979 an agreement was signed between AALCC, the Regional Centre for Commercial Arbitration ((Kuala Lumpur), established by AALCC) and ICSID providing for reciprocal assistance in con-

nexion with proceedings conducted under the auspices of ICSID and the Kuala Lumpur Centre respectively.

74. Another agreement was signed in February 1980 between AALCC, the Regional Centre for Commercial Arbitration (Cairo) and ICSID.

75. As a result of the conclusion of the above two agreements parties may now choose Cairo or Kuala Lumpur as the seat of ICSID conciliation or arbitration proceedings.

76. The Tokyo Maritime Arbitration Commission is expected soon to conclude a co-operation arrangement with the Kuala Lumpur Regional Arbitration Centre to administer international maritime arbitration for the Centre under the UNCITRAL Arbitration Rules.

### C. *Future work on arbitration*

77. At its fourteenth session in October 1980, the Hague Conference on Private International Law decided to include in the agenda of the future work of the Conference the question of the law applicable to arbitration clauses.

### D. *Publication and research*

78. ICC has prepared for publication in 1981 the first volume of the collection entitled *Arbitration Law Throughout the World* as a guide to arbitration law in European countries. The guide will consist of a series of standardized articles summarizing the principal features of relevant legislation in 17 European countries. The second volume will deal with arbitration law in the Far East and the Pacific and will include a description of arbitration law in China, India, Indonesia, Japan, Malaysia, Pakistan, Republic of Korea, the Philippines, Singapore, Sri Lanka, Taiwan and Viet Nam.

79. The Institute of International Business Law and Practice will be publishing an index of arbitration awards "*Lex Mercatoria*". The first step of this project, which consists of publishing the extracts of awards of the ICC Court of Arbitration from 1975 to 1979, will be completed before the end of 1981.

## X. PRODUCTS LIABILITY

80. The Inland Transport Committee of ECE at its thirty-fifth session (ECE/TRANS/18, paragraph 90) in February 1976 requested UNIDROIT to undertake a preliminary study regarding the possibility of preparing a draft Convention on third party liability for damage



caused in the carriage of hazardous substances by road which would aim at establishing "a uniform international application of the principle of third-party responsibility (whether limited or not) of the carrier and possibly the appropriate procedures for compensation". (See VIII. INTERNATIONAL TRANSPORT, B. *Transport over land and related issues*, paragraphs 37-39 above.)

81. For the work of UNIDROIT on the preparation of a Convention relating to liability and compensation for damage caused during the carriage by land of hazardous substances, see paragraphs 37-39 above (VIII. INTERNATIONAL TRANSPORT, B. *Transport over land and related issues*).

82. For the question of liability for damage caused by noise and sonic boom, see paragraph 45 above (VIII. INTERNATIONAL TRANSPORT, C. *Transport by air*).

## XI. PRIVATE INTERNATIONAL LAW

### A. Work of EEC

83. The Convention of the Law Applicable to Contractual Obligations (1980) was concluded by the member States of the European Economic Community on 19 June 1980, at Rome, Italy. It deals with rules applicable "to contractual obligations in any situation involving a choice between the laws of different countries".

### B. Work of the Hague Conference on Private International Law

84. For the work of the Hague Conference on Private International Law, see A/CN.9/202/Add.1, paragraph 1 (I. INTERNATIONAL CONTRACTS, A. *International sales of goods*);\* see also paragraph 108 below (XII. OTHER TOPICS OF INTERNATIONAL TRADE LAW, E. *Sales to consumers*).

### C. Work of ICC

85. An *ad hoc* Working Party set up by the ICC Commission on International Commercial Practice is making recommendations to harmonize the methods that can be utilized in the determination of the law applicable for use of those drawing up contracts and arbitrators. These recommendations define a series of rules governing the general method and designed to establish flexible

presumptions suitable for each category of contract (sale, leasing, distribution, agency services, publishing and building enterprises etc.). The draft is expected to be finalized in May 1981, adopted in June and published in January 1982.

### D. Work of OAS

86. The following are the conventions on conflict of laws signed at Panama, on 30 January 1975 at the Inter-American Specialized Conference on Private International Law.

Inter-American Convention on Conflict of Laws Concerning Bills of Exchange, Promissory Notes and Invoices

Inter-American Convention on Conflict of Laws Concerning Checks

Inter-American Convention on General Rules of Private International Law

Inter-American Convention on Conflicts of Laws Concerning Commercial Companies

### E. Work of UNIDROIT

87. For the work of UNIDROIT, see A/CN.9/202/Add.1, paragraphs 2-4 (I. INTERNATIONAL CONTRACTS, B. *Codification of international trade law*)\* see also paragraphs 88-95 below (XII. OTHER TOPICS OF INTERNATIONAL TRADE LAW, A. *Agency*) and paragraphs 98-103 below (XII. OTHER TOPICS OF INTERNATIONAL TRADE LAW, C. *Protection of the acquisition in good faith of corporeal movables*).

## XII. OTHER TOPICS OF INTERNATIONAL TRADE LAW

### A. Agency

#### 1. Agency: certain aspects of international agency relations in the context of sale of goods

88. The origins of work on this subject date back to studies initiated by UNIDROIT in 1935 which led to the publishing in 1961 of two draft Uniform Laws relating respectively to agency in private law relations of international character and to the contract of commission in the international sale or purchase of goods. In view of the difficulties which this distinction entailed for Common Law countries, where it is unknown, a Committee of Governmental Experts convened by UNIDROIT

\* Reproduced above.

\* Reproduced above.

to end the deadlock suggested narrowing the field in which unification should be attempted and undertook the drafting of a new uniform law dealing with the practical aspects of agency contracts of an international character for the sale and purchase of goods. This Committee met between 1970 and 1972 and adopted the text of the draft uniform law at its fourth and final session. The draft, together with an explanatory report prepared by the Secretariat, was circulated among the member States of UNIDROIT in October 1973, together with a request for information as to whether they would be prepared to take part in a Diplomatic Conference to examine and adopt the draft. Virtually all the replies indicated the willingness of the States in question to participate in such a Conference and in December 1976 the Government of Romania announced its willingness to host the Conference.

89. The draft submitted to the Diplomatic Conference, which was held at Bucharest from 28 May to 13 June 1979, concentrated on a number of questions, namely the sphere of application of the future Convention, the establishment and scope of agency, the relations between the principal and the agent, the legal effects of an act carried out by the agent on behalf of the principal and the termination of agency.

90. One of the principal decisions taken was to extend the scope of application of the draft Convention to cover in principle all intermediaries involved in the conclusion of sales contracts and not just those authorized or purporting to be authorized to conclude such a contract.

91. The chapter of the draft relating to the legal effects of an act carried out by an agent on behalf of the principal, which to some extent sought to reconcile the differences, both conceptual and practical, deriving from the Common Law notion of the undisclosed principal and commission agency as known in countries with a civil law tradition was generally acceptable.

92. The Conference called upon UNIDROIT to take the necessary steps to ensure that the work begun by it be completed as soon as possible and since that time informal consultations have taken place with a view to overcoming the principal outstanding difficulties. With this aim in mind, the Governing Council of UNIDROIT convened a small group of independent experts, representing the Common Law, Civil Law and Socialist systems, to review the progress so far made and to draw conclusions regarding the prospects of future work. This group met in January 1981 and its findings were submitted to the Governing Council of UNIDROIT at its sixtieth session to be held in April 1981. On the basis of the detailed consideration of the conclusions of the group, the Governing Council will take a decision as to the desirability of convening a second Conference to complete work on the agency draft, perhaps in 1982.

## 2. Powers of attorney

93. This subject was placed on the Work Programme of the Institute in 1977 with a view to finding out to what extent differences in the various national laws relating to the forms for granting authority give rise to practical difficulties, in particular in the context of international trade. A detailed study on the existing situation was commissioned by UNIDROIT and an indication of the present position is found in the summary of the report of the consultant expert where he stated the following:

"It emerges clearly from this study that, in connection with the requirements as to form for the granting of authority to agents, there exists in almost all countries a considerable difference between the provisions of the civil law *stricto sensu* and those of commercial law, and this must be borne in mind when contemplating power of attorney."

94. The purpose of this study is to prepare uniform rules governing the validity of powers of attorney to be exercised abroad and, if possible, of a uniform form of power.

95. The study will be circulated. The observations thereon will be considered by a Study Group which will be set up by the Governing Council later on in the course of the triennial period 1981-1983.

## B. Company law

96. The CARICOM Working Party on the Harmonization of Company Law has completed its Report which is accompanied by draft legislation for the implementation of the recommendations in the Report. In the course of its deliberations and in making its recommendations, the Working Party drew heavily upon the experience and research in company law in a number of Commonwealth countries.

97. The Working Party's attention was drawn, *inter alia*, to the extensive growth of off-shore companies in the Caribbean region within recent years. These are companies, which although they are registered in a Member State, are not permitted to operate there, but must carry on their activities substantially outside the State. They are granted specific privileges in relation to tax liabilities and the preservation of the confidentiality of information relating to their operations. These companies are established primarily for the benefits to be gained under the tax laws of metropolitan countries with which they are principally associated. The Working Party on the Harmonization of Company Law was concerned at the possible implications for the Caribbean Community of the growth of off-shore companies especially as they are not restricted by the terms of their establishment from trading in other Member States of the Community. The Working Party's Report contains recommendations for

the regulation of the activities of external companies, but nevertheless, was of the view that the difference in operation of the external company and the off-shore company merited a separate study of off-shore companies being undertaken. The proposal for the study has been approved by the Common Market Council of Ministers and a Working Party on Off-Shore Companies has been established by the Secretary-General of the Caribbean Community for that purpose. The Working Party has so far held three meetings, the last of which was held at Montserrat from 9-12 February 1981.

### C. *Protection of the acquisition in good faith of corporeal movables*

98. The topic governed by the draft uniform law, on which work was completed by a UNIDROIT Committee of Governmental Experts in 1974, is dealt with very differently in the law of the various countries. While the large majority of continental countries base themselves on the principle of the protection of the transferee in good faith, other legal systems, and in particular the Common Law systems, are, on the contrary, based on the opposing principle of the safeguarding of the rights of the dispossessed owner. However, in neither group is the basic principle rigorously applied. The systems which are based on the principle of the protection of the transferee lay down conditions for this protection which often seriously limit its efficacy. On the other hand, the systems which are based on the principle of maintaining the rights of the dispossessed owner also provide exceptions which considerably limit the scope of the principle. These conditions and exceptions vary from country to country. On the whole, the protection given to the transferee in good faith is sometimes extended to all acquisitions, whatever the reason for the owner's dispossession; apart, however, from a few exceptions, most civil law countries exclude the acquisition of movables of which the owner was dispossessed by loss or theft. As for the legal systems which protect the rights of the dispossessed owner, the transferee in good faith is nevertheless protected in certain well-defined cases. In Common Law countries most of these exceptions to the basic principle have been introduced by legislation. There is a tendency to extend the scope of these exceptions, especially as regards trade, and it has been remarked that the exceptions tend to become the general rule in this field.

99. In view of the differences between the aforementioned legal systems, the UNIDROIT Working Committee of Governmental Experts, did not try to draw up a uniform law which would apply to all legal relationships but it restricted unification to international relationships. Moreover, it closely linked the draft to the uniform law on the international sales of goods (ULIS). It considered that ULIS provided a favourable legal basis

for unification in the field of protection of the transferee in good faith and that unification would have a better chance of success if it appeared as a complementary set of rules to ULIS. That was why the Committee restricted the field of application of its draft to acquisitions brought about by a sale within the meaning of ULIS. Moreover, it appeared to the Committee from a comparative study of legal systems, that there was a tendency to protect the transferee in good faith, especially as regards trade relationships. This finding and the argument that the unification of the law of sale and kindred matters aims at promoting international trade, led the Committee to accord extensive protection to the transferee in good faith, even in the case of the acquisition of movables which were stolen from their original owner. The Committee's first concern was therefore to protect the interests of international trade, the certainty of which requires the protection of the transferee.

100. The Governments of the Member States of UNIDROIT reacted favourably to the draft in general. However, some criticisms were put forward. These mainly concerned the linking of the draft to ULIS. The experts agreed with these criticisms and therefore detached the draft from ULIS. Other criticisms concerned the over-emphasis given to the protection of the transferee. These were also considered as being well-founded by the majority of the experts who therefore tried to strike a balance between the interests of the transferee on the one hand and the interests of the dispossessed owner on the other. As a result, the draft received a new orientation which detaches it from the principles which formed the basis of the initial draft.

101. This new orientation is particularly apparent as regards the following questions:

(a) The field of application of the draft is not dependent on that of ULIS. The detachment of the draft from ULIS allowed the experts to extend the application of the draft to acquisitions for value other than those made under an international sale. The acquisitions envisaged do not necessarily refer to the ownership of the movables but may also concern rights *in rem* acquired, for example, by a pledge. Detachment from ULIS led the experts to look for new connecting factors and a territorial connecting factor was chosen, that of the place of the handing over of the movables. However, the field of application of the draft is nevertheless determined by the international character of the relationship in question;

(b) The starting point of the draft is no longer to protect first and foremost the transferee in good faith with a view to promoting trade but rather to look for a fair balance between the interests of the parties concerned. This tendency is manifested in a more subtle regime than that of the initial draft concerning proof of the existence or absence of good faith. However, the

desire to create a fair balance mainly appears in the rules on the acquisition of stolen movables. In the text drawn up by the experts, the transferee may in no case invoke his good faith when acquisition concerns movables of which the owner was dispossessed by theft.

102. This new orientation led the experts to change the title of the draft. The title of the original draft emphasized the fact that it was concerned with the protection of the purchaser. Since the draft is no longer predominantly concerned with the protection of the transferee the title has been changed to "Uniform Law on the Acquisition in Good Faith of Corporeal Movables".

103. Consideration is currently being given to the convening of a Diplomatic Conference for the adoption of the draft Convention, after a final review of its provisions by a Committee of Governmental Experts.

#### *D. Rights of creditors*

104. The CE Working Party of the Committee of experts on the rights of creditors held a meeting in Strasbourg from 28 to 31 January 1980.

105. The Working Party decided to restrict its examination mainly to simple reservation of title. As a basis for its discussions the Working Party agreed that these words should be taken to refer to the agreement concluded between the buyer and the seller of specific (or identifiable goods) whereby the right of property in the goods sold will not pass from the seller to the buyer until the buyer has paid the purchase price of these goods in full.

106. The aim of the Working Party in examining the questions contained in its terms of reference was to find possible and desirable solutions which might be used as a basis for the preparation of an international instrument (Convention or Recommendation). This instrument could have as its aim either a harmonization of national laws in the field of reservation of title or at least the international recognition of reservation of title.

107. In this respect it was agreed that the question of international recognition would arise at least when the goods, which have been sold, are transferred from one Contracting State to another Contracting State.

#### *E. Sales to consumers*

108. The fourteenth session of the Hague Conference on Private International Law adopted some provisions relating to the law applying to certain sales to consumers but without drafting a convention on this subject. However, because of the decision to undertake a general revision of the Hague Convention of 15 June 1955 on the

law applying to sales (see A/CN.9/202/Add.1, paragraph 1), the delegates were of the opinion that no decision should be taken at the present stage concerning the form of the provisions relating to sales to consumers since those provisions could either be included in a special chapter of the future general convention or else be the subject of an independent convention. The delegates to the fourteenth session took the view that it was for the negotiators of the general convention to decide what should be the form of the provisions governing sales to consumers.

109. One of the proposed subjects for inclusion in the CE Medium-Term Plan for 1981-1985 is domestic sale, especially sale to consumers. There is an increasing awareness of the fact that the vendor is at an advantage under the law governing sales as it exists at present in most European States.

110. The various efforts made in a number of States to improve the situation of the purchaser fall into their true perspective at a time when greater social justice is one of the consistent concerns of governments. However, such attempts have been piecemeal and spasmodic. CE hopes to study the problem as a whole, investigating at the European level, a new legal system governing sale that would seek to establish a fairer balance between vendor and purchaser.

#### *F. Consumer protection*

111. CE is making a study of the collective interests of consumers. This involves a study of measures permitting agencies or associations to ensure the legal protection of the collective interest of consumers in member States of CE.

#### *G. Contract guarantees, guidelines on simple demand guarantees and surety contracts*

112. The ICC Commissions on Banking Technique and Practice and on International Commercial Practice are preparing model forms for issuing contract guarantees subject to the ICC's Uniform Rules for Contract Guarantees. The aim for these forms is to encourage wider adoption and correct use of the rules. The model forms are intended for voluntary application by banks and other guarantors. An explanatory brochure on use of the forms is also in the course of preparation.

113. The above ICC Commissions are also preparing guidelines on simple demand guarantees. The aim of this work is to establish guiding principles for the use by banks and other institutions called on to issue guarantees payable on the simple or first demand of the beneficiary without proof of loss or of default in the underlying commercial contract. In particular, the purpose is to

minimize the possibilities of abuse of such guarantees, to the detriment, especially, of the principal.

114. The guidelines will deal essentially with practical problems arising in the operation of simple demand guarantees. The publication of the guidelines will be recommended for adoption by guarantors.

115. CE is making a study on surety contracts on a number of problems arising in international relations.

#### H. Collections

116. The ICC Commission on Banking Technique and Practice is preparing standard forms for use by banks carrying out collection operations subject to the ICC's Uniform Rules for Collections. The aim is to facilitate procedures between banks by providing a standard format. An accompanying explanatory brochure is also in the course of preparation.

117. The Commission is authorized to establish draft forms and explanatory brochure for approval by the ICC Council. The information provided in the forms is intended to be used for instructing banks responsible for carrying out collection operations.

#### I. International factoring

118. The growth of factoring in many parts of the world led the Governing Council of UNIDROIT to include in 1974 on the Work Programme a study on the need for seeking harmonization in this area of the law. Factoring is a technique whereby a supplier of goods or services transfers his short-term commercial claims against his clients to a professional, the factor, who, in return for a commission or premium, ensures their immediate and final settlement, their collection while assuming all the risks of this operation, particularly that of non-payment on the due date owing to the debtor's insolvency, and the management of the assets. In most countries the technique employed for the transfer of debts is that of assignment and few problems have arisen in this context apart from that of the validity of reservation of title clauses.

119. UNIDROIT has concentrated its attention on international factoring as considerable difficulties have been encountered in this field. The Group has so far held one session, in February 1979, and after coming to the conclusion that there was a need for a convention dealing with certain aspects of factoring operations, it suggested that the following points should form the core of such a convention:

(a) Definition of factoring operations (which should, *inter alia*, clearly indicate that only trade debts are contemplated, that it is irrelevant whether the agreement provides for recourse or non-recourse factoring and that

in any event non-notification factoring operations should be excluded);

(b) Scope of application (the convention should only apply to international factoring, the international character residing in the fact that the debt arises under a sale contract or a contract for the provision of service concluded between parties whose places of business are situated in different States);

(c) Formalities for assignment between the supplier and the factor and perhaps also between the import factor and the export factor (need to distinguish the question of the validity of the assignment between the parties and that of its effectiveness vis-à-vis the debtor: whereas its validity between the parties should be subjected only to the requirement that the assignment be in writing, effectiveness vis-à-vis the debtor should be dependent upon notice);

(d) Availability against the factor of defences and rights of set-off which the debtor might have against the supplier (affirmation of the principle that the factor may not have more extensive rights than those of the supplier; determination of the time after which the debtor may no longer set up defences; as regards the substantive rules governing defences, reference to the law applicable to the relations between the supplier and the debtor);

(e) Right of the debtor to recover sums which he ought not to have paid;

(f) Settling of conflicts which may arise between the factor and creditors of the supplier as regards claims of such creditors (refusal to consider either notification or registration in a public register as a means of resolving the conflict; search for some other form of publicity which would be necessary to make the assignment of the supplier's rights to the factor effective against third parties).

120. The Group further decided that the substantive rules in the future Convention should be accompanied by conflicts rules. In its view this solution would at least have the merit of establishing uniform connecting factors in respect of those matters not covered by the uniform law; in this connexion, the Secretariat was requested to enquire into the possibility of co-operation with the Hague Conference on Private International Law.

121. Apart from the Hague Conference, the Commission of the European Communities, the International Chamber of Commerce and a number of associations representing the factoring profession have contributed to the first stages of UNIDROIT's work in this connection.

#### J. International leasing

122. At three sessions, held between November 1977 and October 1980, a UNIDROIT Study Group composed of members from Brazil, France, Nigeria, Switzer-

land, the United Kingdom and the United States of America, worked out a set of preliminary draft rules relating to certain aspects of leasing operations which as is well known, are assuming ever greater importance at both national and international level.

123. The principal features of the rules are their characterization of the *sui generis* form of leasing transaction in which it is the user rather than the owner who chooses both supplier and equipment and their enshrinement of this *sui generis* character in *sui generis* legal consequences framed with its particular characteristics specifically in mind. Thus the uniform rules confer on the user a direct independent right of action for damages against the supplier in respect of any loss or damage sustained by him as a result of non-delivery, late delivery or the delivery of defective equipment. They establish the lessee's right to reject a tender of the equipment which is not made within a reasonable time after the delivery date stipulated in the supply contract (or, if none within a reasonable time after the making of that contract) or which otherwise fails in a material respect to conform to the terms of the supply contract. Both these rights are novel creations in favour of the lessee, as they would normally inure to the lessor as owner of the equipment; their conferment on the lessee in the *sui generis* leasing situation is justified by the fact that it is the lessee who chooses both supplier and equipment. The uniform rules, subject to certain exceptions, on the other hand give the lessor a general immunity from the contractual and tortious duties that would ordinarily flow from his ownership of the equipment, given that this ownership in the *sui generis* form of leasing is stripped of virtually all the normal attributes of legal ownership and that the technical responsibility for the equipment chosen, and therefore the physical risks associated with its use, cannot reasonably be laid at his door.

124. The uniform rules are in no way intended to be an exhaustive regulation of the legal problems arising in respect of this *sui generis* transaction but merely to provide a basic, largely permissive legal framework to which the parties would then be free to add in accordance with the particular requirements of each transaction. This was felt to be particularly important in the case of a transaction to which all the parties are businessmen, consumer leasing having been excluded from the outset.

125. At its third session, the Study Group agreed to limit the scope of the uniform rules to specifically international leasing situations. As regards the question of which factors should determine whether or not a given leasing transaction would be treated as international for the purposes of the uniform rules, it was decided to exclude the impact of the supplier's principal place of business and rather to take the principal places of business of the lessor and the lessee as the decisive factors for this purpose. However, the fact that the uniform

rules are cast in the form of an international Convention and are stated to apply specifically to international leasing situations should not be seen as prejudicing the final form which it may be decided to give the uniform rules. The principal objective of these rules has all along been the establishment of a basic legal framework cast with the particular characteristics of the *sui generis* form of tripartite leasing transaction specifically in mind, so as to distinguish it once and for all from the various classical contractual schemata within the comfortable logic of which it has hitherto in general been the tendency to try to accommodate it. There has been agreement from the outset within the Study Group that, notwithstanding the enormous potential of leasing at the cross-border level, true cross-border leasing will not really take off until such time as there is a greater degree of legal certainty regarding the treatment of leasing transactions at the purely domestic level. Given the dearth of domestic legislation addressed to this problem, it is likely that for some time to come the uniform rules will accordingly have a greater impact as the basis of domestic legislation than as legislation addressed specifically to international leasing.

126. The preliminary draft, illustrated by an explanatory report, was submitted to the UNIDROIT Governing Council scheduled for April 1981, for advice as to the appropriate follow-up action to be taken. On this point it was the feeling of the Study Group that, given the novel nature of the subject-matter, it was perhaps premature to lay this text before Governments at the present time and that it was more important to give it maximum exposure in the world of practice, by the organization of symposia in the various continents.

127. In the meantime, the Study Group has also requested the collaboration of the Hague Conference on Private International Law in revising certain provisions of the preliminary draft which raise questions of private international law.

#### K. Restrictive business practices

##### 1. Set of Multilaterally Agreed Equitable Principles and Rules for the Control of Restrictive Business Practices

128. The United Nations Conference on Restrictive Business Practices approved on 22 April 1980 the Set of Multilaterally Agreed Equitable Principles and Rules for the Control of Restrictive Business Practices (see document TD/RBP/CONF/10) and transmitted it to the General Assembly at its thirty-fifth session. In resolution 35/63 the General Assembly unanimously adopted the Set of Multilaterally Agreed Equitable Principles and Rules for the Control of Restrictive Business Practices and decided to convene, in 1985, under the auspices of UNCTAD, a United Nations Conference to review all aspects of the Set. In addition, it requested the



UNCTAD Trade and Development Board to establish at its twenty-second session (March 1981) an intergovernmental group of experts on restrictive business practices, operating within the framework of a committee of UNCTAD, to provide the ongoing institutional machinery for work in this area.

129. The Set consists, in addition to a Preamble, of seven multilaterally agreed equitable principles for the control of restrictive business practices; principles and rules for enterprises, including transnational corporations; principles and rules for States at national, regional and subregional levels; international measures; and international institutional machinery.

## 2. Model law or laws on restrictive business practices

130. Within UNCTAD work is continuing on the elaboration of a model law or laws on restrictive business practices in order to assist developing countries in devising appropriate legislation. In this connexion the above Set of Principles and Rules calls for States at the national level or through regional groupings to adopt, improve and effectively enforce appropriate legislation and implementing judicial and administrative procedures for the control of restrictive business practices, including those of transnational corporations. Such legislation should be based primarily on the principle of eliminating or effectively dealing with acts or behaviour or enterprises which, through an abuse or acquisition and abuse of a dominant position of market power, limit access to markets or otherwise unduly restrain competition, having or being likely to have adverse effects on their trade or economic development, or which through formal, informal, written or unwritten agreements or arrangements among enterprises have the same impact.

### L. Multinational marketing enterprises

131. Within the framework of UNCTAD's work programme on economic co-operation among developing countries, studies have been prepared that touch on aspects relative to international trade law. In this context, a number of studies have been made on the juridical aspects of multinational marketing enterprises among developing countries.

132. It is envisaged that the work currently under way in UNCTAD in respect to the Global System of Trade Preferences (GSTP) may in due course lead to the preparation of legal texts bearing on the question of international trade law.

### M. Conventions and schemes to promote trade

133. The following instruments have been elaborated by EFTA to facilitate trade in the field of non-tariff barriers:

*Pharmaceutical Inspection Convention* (entered into force on 26 May 1971)

The purpose of the Convention is to facilitate trade in pharmaceutical products, by providing for the recognition of inspections in respect of the manufacture of pharmaceutical products.

The parties to the Convention are the EFTA countries, viz. Austria, Finland, Iceland, Norway, Portugal, Sweden, Switzerland and Liechtenstein, and Denmark, Hungary, Ireland and the United Kingdom.

*Convention on the Control and Marking of Articles of Precious Metals* (entered into force on 27 June 1975)

The purpose of the Convention is to facilitate trade in articles of precious metals (gold, silver and platinum) by providing a Common Control Hallmark.

The parties to the Convention are Austria, Finland, Sweden, Switzerland and the United Kingdom.

*Scheme for the Reciprocal Recognition of Tests and Inspections carried out on Ships' Equipment* (entered into force on 1 January 1971)

The purpose of the scheme is to facilitate trade in ships' equipment by providing for the recognition of tests and inspections thereof.

*Scheme for the Reciprocal Recognition of Tests carried out on Agricultural Machines and Tractors for Operational Safety and Ergonomics and for Road Traffic Safety* (entered into force on 1 September 1972)

The purpose of the scheme is to facilitate trade in agricultural machines and tractors by providing for the recognition of tests and inspections thereof.

*Scheme for the Reciprocal Recognition of Tests and Inspections carried out on Gas Appliances* (entered into force on 1 August 1972)

The purpose of the scheme is to facilitate trade in gas appliances by providing for the recognition of tests and inspections thereof.

*Scheme for the Reciprocal Recognition of Tests and Inspections carried out on Pressure Vessels* (entered into force on 1 January 1971)

The purpose of the scheme is to facilitate trade in pressure vessels by providing for the recognition of tests and inspections thereof.

*Scheme for the Reciprocal Recognition of Tests and Inspections carried out on Lifting Appliances* (entered into force on 1 January 1978)

The purpose of the scheme is to facilitate trade in lifting appliances by providing for the recognition of tests and inspections thereof.



*Scheme for the Reciprocal Recognition of Tests and Inspections carried out on Heating Equipment using Liquid Fuel* (entered into force on 1 January 1978)

The purpose of the scheme is to facilitate trade in heating equipment using liquid fuel by providing for the recognition of tests and inspections thereof.

*Scheme for the Mutual Recognition of Evaluation Reports on Pharmaceutical Products* (entered into force on 13 June 1979)

The purpose of the scheme is to facilitate trade in pharmaceutical products by providing for the recognition of evaluation reports on such products.

#### N. Labour

134. The activities of ILO pertaining to labour and its related aspects are set forth below:

##### 1. *Work directed at the adoption of international labour conventions or recommendations*

135. The following work is directed at the adoption of international labour conventions or recommendations:

##### *Promotion of Collective Bargaining*

It is expected that a Recommendation will be adopted by the International Labour Conference in June 1981.

##### *Equal Opportunities and Equal Treatment for Men and Women Workers: Workers with Family Responsibilities*

It is expected that a Convention and a Recommendation will be adopted by the International Labour Conference in June 1981.

##### *Maintenance of Migrant Workers' Rights in Social Security (Revision of Convention No. 48)*

Proposed conclusions with a view to a Convention and a supplementary Recommendation, based on the consultation of Governments, will be considered by the International Labour Conference in June 1981.

##### *Termination of Employment at the Initiative of the Employer*

Proposed conclusions with a view to a Convention and a supplementary Recommendation, based on the consultation of Governments, will be considered by the International Labour Conference in June 1981.

##### *Vocational Rehabilitation*

A general discussion of the subject by the International Labour Conference in June 1982 is expected to lead to the adoption in 1983 of an instrument

supplementing the Vocational Rehabilitation (Disabled) Recommendation, 1955.

##### *Revision of the Plantations Convention, 1958*

Proposals for a partial revision of the Convention (scope provisions) are to be considered by the International Labour Conference in June 1982.

##### 2. *Preparation of codes of practice, guides and manuals*

136. ILO has prepared the following codes of practice, guides and manuals:

##### *Model Code of Safety Regulations for Industrial Establishments*

Preparatory work for revision is to be carried on during the next two biennia.

##### *Code of Practice on Safety in Haulage and Transport Operations in Mines*

The draft is completed. It is circulated to Governments for comments.

##### *Code of Practice on Safety and Health in the Iron and Steel Industry*

The draft is being prepared. It will be submitted to the Meeting of Experts in December 1981.

##### *Code of Practice on the Safe Use of Diesel-powered Equipment Underground in Mines*

The draft is being prepared.

##### *Code of Practice on Safety and Health in the Construction of Fixed Offshore Installations in the Petroleum Industry*

The draft was completed at a Meeting of Experts recently. It will be published after the approval of the Governing Body.

##### *Code of Practice on Radiation Protection in the Mining and Milling of Radioactive Ores* (Part IV of ILO Manual of Industrial Radiation Protection)

It will be a joint IAEA, ILO and WHO publication.

#### O. *International standards for foods*

137. The thirty-third World Health Assembly (WHO), in resolution WHA33.32, requested the Director-General, *inter alia*, to "prepare an international code of marketing of breastmilk substitutes" and to "submit the code to the Executive Board for consideration at its sixty-seventh session and for forwarding with its recommendations to the thirty-fourth World

Health Assembly, together with proposals regarding its promotion and implementation, either as a regulation in the sense of Articles 21 and 22 of the Constitution of the World Health Organization or as a recommendation in the sense of Article 23, outlining the legal and other implications of each choice". Document EB67/20 (10 December 1980) describes the process of the development of this draft International Code and outlines the legal and other implications of its promotion as a regulation or as a recommendation. The draft International Code itself is presented in the form of a regulation and a recommendation.

#### *P. Most-favoured-nation clause*

138. The topic of the most-favoured-nation clause was first raised in 1964. Then at its nineteenth session in 1967 ILC noted that, at the twenty-first session of the General Assembly, several representatives in the Sixth Committee had urged that ILC deal with the most-favoured-nation clause. In view of the interest expressed in the matter and of the fact that clarification of its legal aspects might be of assistance to UNCITRAL, ILC decided to place on its programme of work the topic of "most-favoured-nation clauses in the law of treaties".

139. In 1968, the Commission instructed a Special Rapporteur to explore the major fields of application of the clause. In 1969, the Special Rapporteur presented his first report.

140. Subsequently, from 1970 to 1976 the Special Rapporteur submitted six more reports dealing with various aspects of the subject. At the twenty-eighth session, in 1976, the Commission completed the first reading of the draft articles on the clause in accordance with the General Assembly's recommendation.

141. At the thirty-first session, the General Assembly by resolution 31/97 of 15 December 1976 recommended that the Commission should conclude the second reading of them in the light of comments received from Member States, from organs of the United Nations which had competence on the subject-matter, and from interested inter-governmental organizations.

142. At the thirtieth session in 1978, the Commission re-examined the draft articles on the basis of the first report submitted by the new Special Rapporteur. Having considered the Special Rapporteur's first report and a number of proposals, as well as the reports of its Drafting Committee, the Commission adopted the final text of a thirty-article draft on most-favoured-nation clauses.

143. By resolution 35/161 of 15 December 1980 on the consideration of the draft articles on most-favoured-nation clauses, the General Assembly requested the Secretary-General to reiterate his invitation to Member

States, organs of the United Nations and interested inter-governmental organizations to submit, or bring up to date, not later than 30 June 1981, their written comments and observations on the draft articles on most-favoured-nation clauses adopted by the International Law Commission. The General Assembly also requested States to comment on the recommendation of the International Law Commission that those draft articles should be recommended to Member States with a view to the conclusion of a convention on a subject.

#### *Q. Jurisdictional immunities of States and their property*

144. One of the areas in which the question of jurisdictional immunities of States and their property arises is that of trading immunities. This topic was included in the provisional list of topics selected for codification by ILC in 1949. However, it was only in 1977 that further consideration was given to it. At its thirty-second session held from 5 May to 25 July 1980, the "Second report on the topic of jurisdictional immunities of States and their property" (A/CN.4/331 and Add.1) was before ILC. Part I of the report deals with questions relating to jurisdictional immunities accorded or extended by territorial States to foreign States and their property. Part II examines State practice—judicial, administrative and governmental—relating to the fundamental principles of international law of State immunities. It may be noted that UNCITRAL deferred the consideration of this subject in relation to arbitration pending the outcome of the work by ILC.

#### *R. Proposed treaty for the establishment of a preferential trade area for eastern and southern African States*

145. ECA has proposed a treaty for the establishment of a preferential trade area for eastern and southern African States. This proposed Treaty was submitted for consideration at the second Extraordinary Conference of Ministers of Trade, Finance and Planning of the eastern and southern African States, Kampala, Uganda, from 27 October to 1 November 1980. This draft Treaty is still the subject of negotiations.

#### *S. GATT's new programme of work*

146. In 1979 GATT adopted a new programme of work which will be the basis of its activities in the 1980s. The implementation of the Tokyo Round agreements is a major element of this work programme, but in addition

the Contracting Parties have agreed to continue work in the following areas:

**Agriculture:** Questions relating to trade in agricultural products are to continue to be an important part of the work of GATT

**Safeguards:** Negotiations on safeguards are to be continued as a matter of urgency

**Continuation of the process of trade liberalization**

**Structural adjustment and trade policy:** The Consultative Group of Eighteen, which has been established as a permanent body of GATT, has been requested to pursue the examination of the problems of structural adjustment and trade policy taking into account trade relations between North and South

**GATT and developing countries:** By giving priority to trade issues of interest to developing countries and by strengthening the role of the GATT Committee on Trade and Development, the Contracting Parties expect to make a contribution to the satisfactory solution of the problems highlighted in the report of the Brandt Commission. In parallel with the establishment of the Safeguards Committee, the Contracting Parties have also established a Sub-Committee on Protective Measures which will examine new measures of protection affecting the trade of developing countries. GATT also intends to continue efforts aimed at promoting further expansion of trade among developing countries. The technical assistance activities of the GATT secretariat are to be continued.

### XIII. FACILITATION OF INTERNATIONAL TRADE

#### A. *Facilitation of international trade procedures*

##### 1. *Trade data elements directory*

147. The ECE Committee on the Development of Trade (Working Party on Facilitation of International Trade Procedures) has prepared the Trade Data Elements Directory (TRADE/WP.4/133) which includes agreed sets of standard data elements which are intended to facilitate interchange of data in international trade. These standard data elements can be used with any method for data interchange—on paper documents as well as with other means of data communication.

148. At present, data elements in the following areas have been recommended: maritime and combined transport; commercial invoice and related documents; road transport; customs applications; rail transport; and documentary credits. It is expected that the Directory will be completed in 1981. In March 1981, the ECE Working Party on Facilitation of International Trade Procedures recommended data elements in the following areas: multimodal transport; air transport; and freight

forwarding. The Directory will be maintained by the Working Party in accordance with agreed rules.

149. This project comprises the standardization of data elements contained in those documents which have been used in international trade. These elements correspond in substance to proposed ISO International Standards. The legal issues involved in this project therefore are those which generally appear in connexion with trade facilitation, i.e. document form; authentication; negotiability; security; import procedures; trade terms; certificates required by national law; and other documentation.

150. The Directory may be considered as a set of non-mandatory recommendations available for use by participants in international trade. The project is being implemented in co-operation with UNCTAD; International Chamber of Commerce (ICC); International Chamber of Shipping (ICS); International Organization for Standardization (ISO); Inter-governmental Maritime Consultative Organization (IMCO); Customs Co-operation Council (CCC); International Federation of Freight Forwarders Associations (FIATA); International Railway Transport Committee (CIT); European Economic Community (EEC); International Air Transport Association (IATA); International Road Transport Union (IRU); Central Office for International Railway Transport (OCTI); Society for Worldwide Interbank Financial Telecommunication S.C. (SWIFT); United Nations Statistical Commission; International Union of Railways (UIC); national facilitation organs and focal points for trade facilitation work; and other bodies. Such co-operation has proved to be advantageous in the areas of concern (trade facilitation, trade terms, standards, shipping, etc.) to each of the organizations and bodies listed.

151. The Directory was adopted by the Working Party on Facilitation of International Trade Procedures at its twelfth session held from 25 to 26 September 1980. It was adopted by representatives of the following ECE member countries: Austria, Belgium, Bulgaria, Canada, Czechoslovakia, Denmark, Finland, France, German Democratic Republic, Germany, Federal Republic of, Hungary, Netherlands, Norway, Poland, Romania, Spain, Sweden, Switzerland, Turkey, USSR, United Kingdom and the United States.

##### 2. *Trade data interchange*

152. In 1975 the ECE Committee on the Development of Trade (Working Party on Facilitation of International Trade Procedures) set up a task team which prepared "Guidelines for trade data interchange developed within ECE". The Guidelines will be issued shortly. However, in view of current opinion that there will be more than one way of exchanging data and that trading partners will be able to choose between them, the working Party decided—instead of having one single

common message structure system—to register and publish the main message structure systems in actual practice. Rules for the registration of such systems are to be developed, and registered systems will be contained in a future international trade protocol directory. A first draft of the rules for registration of systems in the future international trade protocol directory was discussed in March 1981.

153. The Guidelines for trade data interchange developed within the ECE were approved for publication by the Working Party on Facilitation of International Trade Procedures at its ninth session in 1979 (TRADE/WP.4/127).

### 3. Alignment of trade documents

154. The ECE Committee on the Development of Trade (Working Party on Facilitation of International Trade Procedures) is engaged in a project dealing with the alignment of trade documents. This includes harmonization and simplification of international trade documents such as the multimodal transport document, piggy-back transport note, universal air waybill, universal (multi-purpose) transport document, control certificates, commercial contracts, forwarding instructions, and phytosanitary certificates. Both harmonization and simplification are based on the United Nations Layout Key for Trade Documents. The project embodies the United Nations system of aligned trade documents, work on the completion and maintenance of which is continuing.

155. The project is being carried out in co-operation with the Inter-governmental Maritime Consultative Organization (IMCO); Customs Co-operation Council (CCC); Central Office for International Railway Transport (OCTI); International Monetary Fund (IMF); Council for Mutual Economic Assistance (CMEA); European Economic Community (EEC); International Chamber of Commerce (ICC); International Federation of Freight Forwarders Association (FIATA); International Road Transport Union (IRU); International Union of Railways (UIC); International Organization for Standardization (ISO); International Chamber of Shipping (ICS); International Railway Transport Committee (CIT); International Union of Combined Rail/Road Transport Companies (UIRR). The final text of the recommendation is under preparation.

156. In the framework of the CMEA Standing Commission on Foreign Trade work is continuing on the simplification and standardization of documents in the sphere of foreign trade.

#### B. Trade facilitation information

157. At its eleventh session in March 1980, the Working Party on Facilitation of International Trade

Procedures, a subsidiary of the Committee on the Development of Trade of ECE, agreed to issue an information leaflet "Facts about the Working Party on Facilitation of International Trade Procedures" (TRADE/WP.4/INF.68; TD/B/FAL/INF.69).

### XIV. ACCESS TO JUSTICE AND VALIDITY OF FOREIGN JUDGMENTS AND ARBITRAL AWARDS

#### A. Mutual judicial assistance

158. The fourteenth session of the Hague Conference (October 1980) adopted a *Convention for the Purpose of Facilitating International Access to Justice*. This Convention deals with questions of judicial assistance, *cautio judicatum solvi*, copies of writs and court orders, imprisonment for debt and safe-conduct (actually this is a matter of revising chapters III to VI of the 1954 Hague Convention on Civil Procedure). The Convention was immediately opened for signature and is dated 25 October 1980; on that date it had been signed by three States, namely, France, Germany, Federal Republic of, and Greece.

#### B. Inter-American Convention on Extraterritorial Validity of Foreign Judgements and Arbitral Awards

159. The Inter-American Convention on Extraterritorial Validity of Foreign Judgements and Arbitral Awards was signed at Montevideo, Uruguay, on 8 May 1979 at the Second Inter-American Specialized Conference on Private International Law.

### XV. TRAINING AND RESEARCH ON ISSUES CONCERNING THE ESTABLISHMENT OF THE NEW INTERNATIONAL ECONOMIC ORDER

160. Since 1975, in response to the policies adopted by the General Assembly, UNITAR's programme of work has placed special emphasis on issues concerning the establishment of the new international economic order. Some of the documents, based on projects relating to the new international economic order, which have been prepared are:

Third Progress Report on Technology, Domestic Distribution and North-South Relations

Obstacles to the New International Economic Order: an Overview

International Development in the 1980s and Beyond: Essential Requirements and Industrialized Country

Responses (Report of a Task Force on International Development)

Conclusions of the UNITAR-Club of Rome-CEESTEM Conference on Regionalism and the New International Economic Order.

161. Another project examines the structure and pattern of six international commodity markets—in food, energy, raw materials, capital goods, manufactured goods and armaments—to determine how they facilitate or impede the emergence and pursuance of rational policies designed to optimize the use of local resources, human or material. For this purpose the tools of analysis (a model and scenarios) are adjusted to study the impact of the six commodity markets within different regions.

162. The UNITAR Project on the Future has been organizing a series of major regional conferences, the first of which on "Africa and the Problematique of the Future" was held in 1977 at Dakar, Senegal. A second conference on "Alternative Development Strategies and the Future of Asia" was held in March 1980 at New Delhi, India. These conferences have involved scholars, planners and government officials in a dialogue on the evolution of development alternatives rooted in the particular circumstances of the region.

163. In collaboration with CEESTEM, UNITAR has organized and co-ordinated a network of 98 teams of independent researchers in all parts of the world. Each unit of the network has (i) assessed the feasibility of implementing the relevant new international economic order objectives in the researcher's region, or nation, or sector of expertise; (ii) reported on official positions concerning the objectives as well as responses and attitudes by other socio-economic strata (business, labour, media, general population, etc.); and (iii) suggested feasible strategies or modes of implementation.

164. The research findings of the entire network are published in 17 volumes in the UNITAR-CEESTEM Library on the new international economic order. The main issues of the new international economic order covered in this series include:

Aid and assistance targets and the structural and functional parameters of official development assistance (ODA) transfers

International trade, including issues pertaining to tariff and non-tariff barriers, the generalized system of preferences, commodities, agricultural and general trade, and the insertion of developing countries into the world economy

International finance covering such issues as the reform of the voting structure of the International Monetary Fund (IMF), debt renegotiation and servicing, SDRs and private and capital flows

Industrialization, technology transfer and business practices, including developed and developing country perspectives on redeployment of industry, the creation of a code of conduct for transnational corporations, the competitiveness of natural resources vis-à-vis synthetics, and the legal framework required to end restrictive business practices

Social and cultural issues, focusing on the achievement of a more equitable distribution of income, providing health services and education and welfare for children

Political and institutional issues, covering the economic sovereignty of States and the positions of various member nations on the proposals and objectives of the new international economic order.

165. The call for a new international economic order has strained the capacity of the United Nations system and has led to reform efforts to make it a better vehicle for negotiating and implementing the new order. These reform efforts are the focus of this UNITAR project, which will result in two publications. The first is a policy-oriented monograph focusing on institutional adaptations, including the interplay between the substantive agenda and the institutional context within which it is being promoted and negotiated.

166. The second publication will describe and analyse aspects of the new international economic order negotiating process, mainly from the perspectives of participants in that process. It will contain 18 original essays which address some of the issues in the North-South dialogue under the following four themes:

(a) Negotiating the new international economic order

Institutional elements in the new diplomacy for development

The confidence factor in multilateral diplomacy

The experience of the Conference on International Economic Co-operation

The United Nations conference system and the quest for the new international economic order

Negotiating the UNCTAD Common Fund

Negotiating the regime of the sea-bed;

(b) The new international economic order and the group system

The new international economic order dialogue and the group system

The role of the non-aligned States in creating the new international economic order

Strengthening the negotiating capacity of the Group of 77;

(c) Institutional change

Adapting old order institutions to new order diplomacy

Decision-making in UNESCO: experiment with the drafting and negotiating group

Alternatives in multilateral decision-making

The restructuring exercise of the United Nations;

(d) The institutional agenda and the new international economic order

UNCTAD and the new international economic order

The Law of the Sea Conference and the new international economic order

The new international economic order and transnational corporations

The new international economic order and technical co-operation among developing countries

The unfinished institutional agenda of the new international economic order.

167. The Centre for Research on the New International Economic Order is engaged in carrying out studies on the legal aspects of NIEO as identified by ILA's Committee on NIEO. A seminar was held at Oxford in March/April 1981. The following topics were discussed:

(a) General principles and the Charter of Economic Rights and Duties of States, including conceptual and institutional issues;

(b) Subjects referred to in Article 2 of the Charter of Economic Rights and Duties of States relating to permanent sovereignty over natural resources, wealth and economic activities, in particular:

Measures for international co-operation (particularly dispute settlement and bilateral and other treaties of co-operation)

Application of principle (j) set out in Chapter 1 ("fulfilment in good faith of international obligations")

Standards for payment of "appropriate compensation";

(c) Transnational corporations and in particular codes of conduct and guidelines for transnational corporations;

(d) Transfer of technology;

(e) Restrictive business practices;

(f) International trade with reference to NIEO objectives:

Legal implications of new codes which emerged from the Multilateral Trade Negotiations for developing countries and proposals relating to the promotion of NIEO objectives

Consideration of rule-making, complaint and dispute-settlement procedures in trade codes (existing and proposed)

Legal aspects of proposals for a new International Trade Organization;

(g) Legal aspects of the global food distribution and utilization in a new international economic order;

(h) Contracts in the field of industrial development;

(i) Legal aspects of international monetary and financial reform;

(j) Right to development.

[A/CN.9/202/Add.3\*]

### **Recent and current activities of the International Law Commission which may bear upon questions related to the field of international trade law**

By resolution 34/142 of 17 December 1979\*\* the General Assembly requested the Secretary-General "to take effective steps to secure a close co-ordination, especially between those parts of the Secretariat which are serving . . . the International Law Commission . . ."

Accordingly, the Secretary of the United Nations Commission on International Trade Law (UNCITRAL) by memorandum LE 133 (1-1) dated 6 November 1980, requested the Secretary of the International Law Commission (ILC) to provide detailed information on its recent and current activities in the field of international trade law for inclusion in the Secretary-General's report to be submitted to the fourteenth session of UNCITRAL in June 1981.

In response to the memorandum, the Enlarged Bureau and the Planning Group of ILC at a meeting in May 1981, authorized the Secretary of ILC to provide information on its recent and current activities which may bear upon questions related to the field of international trade law. This information is reproduced in the annex to this document.

## **ANNEX**

### *A. General observations*

1. By resolution 174 (II) of 21 November 1947, the General Assembly of the United Nations established the International Law Commission and approved its Statute. Article 1, paragraph 1, of the Statute<sup>1</sup> states that "The International Law Commission shall have for its object the promotion of the progressive development of international law and its codification". Paragraph 2 of article 1 of the

\* 5 June 1981. Incorporates A/CN.9/202/Add.3/Corr.1 (English only) (17 June 1981).

\*\* Yearbook . . . 1980, part one, I, C.

<sup>1</sup> A/CN.4/1/Rev.1.

Statute stipulates that "The Commission shall concern itself primarily with public international law, but is not precluded from entering the field of private international law" (emphasis supplied).

2. In 1965, in connexion with the examination of an item entitled "Consideration of steps to be taken for progressive development in the field of private international law with a particular view to promoting international trade", the Sixth Committee included in its report to the General Assembly the following passage:

"It was agreed that consultations with the International Law Commission, other United Nations organs and autonomous institutions should be conducted informally by the Secretary-General".<sup>2</sup>

3. The Commission at its 880th meeting, on 29 June 1966, discussed the question<sup>3</sup> of the responsibilities of United Nations organs in furthering co-operation in the development of the law of international trade in promoting its progressive unification and harmonization.<sup>4</sup> At the conclusion of the discussion, the representative of the Secretary-General, the Legal Counsel, "noted that there was clearly a consensus of opinion in the Commission that it should not undertake a responsibility for studying the topic in question."<sup>5</sup>

4. In a report submitted to the twenty-first session of the Assembly, the Secretary-General stated that

"... the views of the Commission were sought as to whether it would be in a position to undertake additional responsibilities in the area of international trade law. The Secretary-General has been advised that, in the view of its manifold activities and responsibilities and considering its extensive agenda, the Commission does not believe that it would be appropriate for it to become responsible for work in the field of the progressive development of the law of international trade."<sup>6</sup>

This indication from the Commission was also reflected in the report of the Sixth Committee to the General Assembly<sup>7</sup> which recommended the adoption of resolution 2205 (XXI) of 17 December 1966,\* establishing the United Nations Commission on International Trade Law (UNCITRAL).

5. The Commission's most recent pronouncement concerning its work in the public and private fields of international law is contained in its observations on the item "Review of the multilateral treaty-making process" approved at its thirty-first (1979) session and submitted to the General Assembly:

"10. ... Article 1, paragraph 2, of the Statute states that the Commission 'shall concern itself primarily with public international law'.<sup>8</sup> The Commission has, therefore, been invested by the General Assembly with general permanent functions in its own field of activity, as defined by its Statute, occupying in that respect a central position within the United Nations system in the task of assisting the General Assembly in the promotion of the progressive development of international law and its codification.

"11. Other subsidiary organs set up within the United Nations have also been entrusted with functions aimed at or resulting in the promotion of the progressive development of international law and its codification by the United Nations. The United Nations Commission on International Trade Law (UNCITRAL), the Legal Subcommittee of the Committee on the Peaceful Uses of Outer Space,

the Commission on Human Rights could be mentioned as examples of bodies established on a permanent basis and dealing with questions of international law or matters relevant thereto. ... A point common to all the above-mentioned permanent or *ad hoc* bodies is that their contributions to the progressive development of international law and its codification take place in specific fields as defined in their mandates. Article 18 of the Statute of the Commission provides that it shall survey 'the whole field of international law with a view to selecting topics for codification'. Moreover, the General Assembly has referred, in the course of the years, to the Commission for consideration topics belonging to various fields of international law ...

"5 During its first thirty-one sessions, however, the Commission, with the endorsement of the General Assembly, has worked almost exclusively in the field of public international law." (emphasis supplied)<sup>9</sup>

## B. Recent activity of the Commission

6. The International Law Commission recently concluded its work on one topic (The most-favoured-nation clause) which may be considered as bearing on questions related to the field of international trade law. That being so, the material that follows with respect to that topic lends itself to being presented, for the most part, within the organizational framework suggested in the letter of 5 November 1980 addressed to various organizations by the Secretary of UNCITRAL. However, the Commission's work as it relates to questions which have a bearing on the field of international trade law is not limited to one area of international law. In section C below, an indication is given of work presently being undertaken with regard to other topics on the Commission's agenda which may be relevant. It may well be that UNCITRAL would be in the best position to ascertain the extent to which the Commission's work on these and other topics has an impact on the questions related to the field of international trade law.

### 1. Subject of project

7. The "project" was work on the topic "The most-favoured-nation clause". That work is described, and the results thereof reflected, in Chapter II of the report of the International Law Commission on the work of its thirtieth (1978) session.<sup>9</sup>

### 2. Authorizing or initiating bodies and terms of reference

8. The topic first appeared on the programme of work of the Commission in 1967 as a result of a Commission decision reflected in its 1978 report as follows:

"At its nineteenth session, in 1967, the Commission noted that, at the twenty-first session of the General Assembly, several representatives in the Sixth Committee had urged that the Commission should deal with the most-favoured-nation clause as an aspect of the general law of treaties. In view of the interest expressed in the matter and of the fact that clarification of its legal aspects might be of assistance to UNCITRAL, the Commission decided to place on its programme of work the topic of 'most-favoured-nation clauses in the law of treaties' ..."<sup>10</sup>

At its 1968 session, the Commission shortened the title of the topic to "The most-favoured-nation clause".

\* Yearbook ... 1968-1970, part one, II, E.

<sup>2</sup> Official Records of the General Assembly, Twentieth Session, Annexes, agenda item 12, doc. A/6206, para. 18.

<sup>3</sup> See ILC (XCIII) MISC.2.

<sup>4</sup> Yearbook of the International Law Commission, 1966, vol. I, part II, pp. 249-252, 880th meeting, paras. 38-66. The question is also briefly referred to in the report of the Commission on the work of its eighteenth session, Yearbook ... 1966, vol. II, p. 173, doc. A/6309/Rev. 1, part II, para. 8.

<sup>5</sup> Yearbook ... 1966, vol. I, part II, p. 252, 880th meeting, para. 66.

<sup>6</sup> Official Records of the General Assembly, Twenty-first Session, Annexes, agenda item 88, doc. A/6396, para. 5.

<sup>7</sup> Ibid., doc. A/6594, para. 5.

<sup>8</sup> A/35/312/Add.2 and Corr.1, to be reproduced in Yearbook ... 1979, vol. II (Part One), doc. A/CN.4/325.

<sup>9</sup> Yearbook ... 1978, vol. II (Part Two), doc. A/33/10.

<sup>10</sup> Ibid., p. 8, para. 16 (emphasis added). The topic was first discussed in the Commission in 1964 when one of its members proposed the inclusion of a provision on the most-favoured-nation clause in the draft articles on the law of treaties then under preparation. While the Commission, after examining the proposal, considered that it would not be advisable to deal with the most-favoured-nation clauses in the codification of the general law of treaties, it thought they might at some future time appropriately form the subject of a special study. Ibid., para. 15.



9. The General Assembly, having considered the 1967 report of the Commission, recommended in its resolution 2272 (XXII) of 1 December 1967 that the Commission study the topic. From that time on, the topic was normally inscribed on the Commission's agenda until completion of the project in 1978. The Assembly during that period recommended that the Commission continue its study of the topic (1968 to 1972), proceed with the preparation of draft articles on the topic (1973 and 1974), complete the first reading of those articles (1975) and complete the second reading of those draft articles; in the light of comments received from Member States, from organs of the United Nations which had competence on the subject-matter and from interested inter-governmental organizations (1976 and 1977). By part II of its resolution 33/139 of 19 December 1978 the Assembly expressed its appreciation to the Commission for its valuable work on the most-favoured-nation clause and to the Special Rapporteurs on the topic for their contribution to this work.

10. As to the terms of reference or scope of the project, the Commission explained as follows in its 1978 report:

"60. As already noted, the idea that the Commission should undertake a study of the most-favoured-nation clause arose in the course of its work on the law of treaties. The Commission considered that, although the clause, conceived as a treaty provision, fell entirely under the general law of treaties, it would be desirable to make a special study of it. While recognizing that there was particular interest in taking up that study because of the attention devoted to the clause as a device frequently used in the *economic sphere*, it understood its task as being to deal with the clause as an aspect of the law of treaties. When it first discussed the question on the basis of the preparatory work of the Special Rapporteur in 1968, the Commission had decided to concentrate on the legal character of the clause and the legal conditions of its application, in order that the scope and effect of the clause as a legal institution might be clarified.

"61. The Commission maintains the position it took in 1968 and points out that the fact that the title of the topic was changed from 'most-favoured-nation clauses in the law of treaties' to the 'most-favoured-nation clause' did not indicate any change in its intention to deal with the clause as a legal institution and to explore the rules of law pertaining to the clause. The Commission's approach has remained the same: while recognizing the fundamental importance of the role of the most-favoured-nation clause in the *domain of international trade*, it did not wish to confine its study to the operation of the clause in that sphere but to extend the study to the operation of the clause in as many spheres as possible.

"62. The Commission has been cognizant of matters relating to the operation of the most-favoured-nation clause in the *sphere of international trade*, such as the existence of the General Agreement on Tariffs and Trade, the emergence of State-owned enterprises, the application of the clause vis-à-vis quantitative restrictions and the problem of the so-called 'anti-dumping' and 'countervailing' duties. The Commission has attempted to maintain the line it set for itself between law and economics, so as not to try to resolve questions of a technical economic nature, such as those mentioned above, which pertain to areas specifically assigned to other international organizations.

"63. On the other hand, although it was not the Commission's intention to deal with matters pertaining to areas specifically assigned to other international organizations, it wished to take into consideration all modern developments that might have a bearing upon the codification or progressive development of rules relating to the operation of the clause. In that connexion, the Commission devoted special attention to the question of the manner in which the need of developing countries for preferences in the form of exceptions to the most-favoured-nation clause in the sphere of economic relations could be given expression in legal rules."<sup>11</sup>

### 3. Legal issues involved in the project

11. The legal issues addressed are spelled out in general in the paragraphs immediately quoted above. A more detailed indication of the legal issues dealt with in the Commission's draft may be found by examining the titles to the Commission's thirty draft articles on most-favoured-nation clauses as finally adopted in 1978.

### 4. Course of action contemplated

12. At its 1522nd meeting, on 20 July 1970, the International Law Commission decided, in conformity with article 23 of its Statute, to recommend to the General Assembly that the draft articles on most-favoured-nation clauses should be recommended to Member States with a view to the conclusion of a convention on the subject.<sup>12</sup>

### 5. Difficulties encountered

13. While they should not be termed "difficulties", the Commission had before it certain proposals submitted by members which were not included in the final set of draft articles for various reasons. The titles of those proposals suggest their subject-matter:

Article A. The most-favoured-nation clause and treatment extended in accordance with the Charter of Economic Rights and Duties of States<sup>13</sup>

Article 21 *ter*. The most-favoured-nation clause and treatment extended under commodity agreements<sup>14</sup>

Article 23 *bis*. The most-favoured-nation clause in relation to treatment extended by one member of a customs union to another member<sup>15</sup>

Article 28. Settlement of disputes and Annex<sup>16</sup>

14. Note may also be taken of the remark in paragraph (15) of the commentary to article 24 dealing with "The most-favoured-nation clause in relation to arrangements between developing countries" that some Commission members believed that the absence of agreed concepts of developed and developing States, in particular for purposes of international trade, might give rise to enormous difficulties in the application of the provisions of article 24.<sup>17</sup>

### 6. Other organizations or bodies in collaboration with which the project was carried out

15. As indicated in paragraph 9 above, the General Assembly, by resolution 31/97 of 15 December 1976, requested the International Law Commission to complete at its 1978 session the second reading of its draft article on the most-favoured-nation clause, in the light of comments received not only from Member States, but also from organs of the United Nations which had competence on the subject-matter and from interested inter-governmental organizations.

16. At its 1977 session, the Commission instructed the Secretariat to transmit the draft articles to the United Nations bodies, specialized agencies and inter-governmental organizations indicated in the standard list used by UNCTAD.<sup>18</sup> Thus, the Secretariat transmitted the draft articles for comment to some 13 United Nations bodies, 15 specialized or related agencies and 58 other inter-governmental organizations.

17. Comments were received for consideration by the Commission at its 1978 session from the following organs, agencies and organizations: Economic Commission for Europe, Economic Commission for Western Asia, United Nations Conference on Trade and Development, United Nations Educational, Scientific and Cultural Organi-

<sup>12</sup> *Ibid.*, p. 16, para. 73.

<sup>13</sup> See *ibid.*, p. 13, para. 55.

<sup>14</sup> See *ibid.*

<sup>15</sup> See *ibid.*, pp. 13-14, paras. 56-58.

<sup>16</sup> See *ibid.*, p. 15, paras. 68-69.

<sup>17</sup> *Ibid.*, p. 68.

<sup>18</sup> Yearbook . . . 1977, vol. I, p. 237, 1458th meeting, paras. 33-36.

<sup>11</sup> *Ibid.*, p. 14, paras. 60-63 (emphasis added).

zation, International Atomic Energy Agency, General Agreement on Tariffs and Trade, Board of the Cartagena Agreement, Caribbean Community Secretariat, European Economic Community, European Free Trade Association, Latin American Free Trade Association, League of Arab States and World Tourism Organization.<sup>19</sup>

#### 7. Work of other organizations engaged in similar projects

18. While it would appear no inter-governmental organizations were engaged in the preparation of draft articles on most-favoured-nation clauses at the time the Commission was so engaged, such organizations as GATT (multilateral trade negotiations), UNCTAD (including its Special Committee on Preferences), free trade organizations and customs unions were obviously active in fields related to the clause or to its application. These activities were brought to the attention of the Commission by the first Special Rapporteur on the topic in his reports submitted to the Commission<sup>20</sup> as well as by the organizations themselves and Member States in their comments submitted on the Commission's provisional draft articles (see para. 17 above). As far as non-governmental organizations are concerned, the Special Rapporteur in his reports, one Member State and one inter-governmental international organization in their comments, referred to resolutions adopted by the Institute of International Law, as well as to reports and studies undertaken for the Institute.

#### 8. The final text

19. The final text of the draft articles on most-favoured-nation clauses was adopted by the International Law Commission at its 1523rd meeting, held on 21 July 1978.

20. As noted above in paragraph 13, the Commission recommended to the General Assembly in 1978 that it recommend the draft articles to Member States with a view to the conclusion of a convention on the subject. By part II of resolution 33/139 of 19 December 1978, all States, organs of the United Nations having competence in the subject-matter and interested inter-governmental organizations were invited to submit their written comments and observations on chapter II of the 1978 Commission report and, in particular, on (i) the draft articles on most-favoured-nation clauses adopted by the Commission; and (ii) those provisions relating to such clauses on which the Commission was unable to take decisions. In addition, States were requested to comment on the recommendation that the draft articles be recommended to Member States with a view to the conclusion of a convention on the subject. At its thirty-fifth (1980) session, the General Assembly had before it in response to that invitation, the comments and observations submitted by eighteen Governments and five inter-governmental organizations, as well as an analytical compilation of those comments and observations (A/35/203 and Add.1-3; A/35/443). On 15 December 1980, the Assembly, aware of the fact that more replies were needed, adopted resolution 35/161 reiterating the invitation contained in resolution 33/139 and including in the pro-

visional agenda of its 1981 session an item entitled "Consideration of the draft articles on most-favoured-nation clauses".

#### C. List of matters possibly of interest to UNCITRAL

21. The Commission's agenda for its present, thirty-third session does not appear to include topics directly related, as such, to the "List of matters of interest to UNCITRAL" attached to the letter of 5 November 1980 referred to earlier.

22. It might be noted, however, that included in the draft articles on *succession of States in respect of matters other than treaties*, adopted on first reading by the Commission at its 1979 session,<sup>21</sup> is a part II relating to the effects of a succession of States in respect of State property and a part III relating to the effects of a succession of States in respect of State debts. A definition of "State debt" is included in the draft (article 16) and provides that for the purposes of the articles in part III of the draft, "State debt" means: (a) any financial obligation of a State towards another State, an international organization or any other subject of international law; (b) any other financial obligation chargeable to a State". At its present session the Commission intends to complete the second reading of those draft articles, as recommended by the General Assembly in resolution 35/163 of 15 December 1980.

23. At its 1980 session the Commission adopted on first reading a set of draft articles on *treaties concluded between States and international organizations or between international organizations*.<sup>22</sup> Article 1 provides that the articles apply to (a) treaties concluded between one or more States and one or more international organizations, and (b) treaties concluded between international organizations. Included in the article on use of terms (article 2) is a provision indicating that for the purposes of the articles, "treaty" means an international agreement governed by international law and concluded in written form: (i) between one or more States and one or more international organizations, or (ii) between international organizations—whether that agreement is embodied in a single instrument or in two or more related instruments and whatever its particular designation." Thus, treaties as defined by that provision between States and international organizations or between international organizations which concern *inter alia* trade, economic and commercial questions (such as "multilateral commodity agreements") are included within the scope of those draft articles. At its present session, the Commission has commenced, pursuant to resolution 35/163, the second reading of these draft articles.

24. In connexion with the topic of *State responsibility*, it may be noted that in the preparation of draft articles on the responsibility of States for internationally wrongful acts, the Commission has adopted in first reading a draft article (article 31) entitled "*Force majeure and fortuitous event*" as a circumstance precluding wrongfulness, in part one of the draft relating to "the origin of international responsibility". The text of that draft article and commentary thereto are found in the 1979 report of the Commission.<sup>23</sup> As a general matter it might be useful to recall that the draft articles on this topic relate to the international responsibility of a State for every internationally wrongful act committed by that State (article 1). This would obviously include internationally wrongful acts committed in breach of an international obligation of a State related to international trade law matters. In accordance with resolution 35/163, the Commission intends to continue its work on the topic with the aim of beginning the preparation of draft articles concerning part two (content, forms and degrees of international responsibility) of the draft, bearing in mind the need for a second reading of the draft articles constituting part one of the draft.

<sup>19</sup> See Yearbook . . . 1978, vol. II (Part Two), p. 161, document A/33/10, Annex.

<sup>20</sup> In his report (Yearbook . . . 1969, vol. II, doc. A/CN.4/213), the Special Rapporteur reviewed attempts at codification under the aegis and in the era of the League of Nations. In his second report (Yearbook . . . 1970, vol. II, doc. A/CN.4/228 and Add.1), he reviewed the experience of international organizations and interested organizations in the application of the clause. In the field of international trade section, particular attention was paid to the structure, principles or activities of such organizations as UNCTAD, GATT, the Economic Commission for Europe, the Latin American Free Trade Association, and the European Free Trade Association. In later reports containing proposed draft articles, the Special Rapporteur had occasion to refer to the activities of organizations reflected in his first and second report, sometimes up-dated, as well as to the views and practice of the European Economic Community. In preparing his reports, the Special Rapporteur had at his disposal research and other materials furnished by the Secretariat which related, *inter alia*, to the activities of the above-mentioned organizations.

<sup>21</sup> For the text of these articles and commentaries thereto, see Yearbook . . . 1979, vol. II (Part Two), p. 40, chapter II.B.

<sup>22</sup> Official Records of the General Assembly, Thirty-fifth Session, Supplement No. 10 (A/35/10), p. 139, chapter IV.B.

<sup>23</sup> Yearbook . . . 1979, vol. II (Part Two), p. 122, doc. A/34/10, chapter III.B.2.

25. The Commission, at its 1980 session, held an exchange of views on the topic "*International liability for injurious consequences arising out of acts not prohibited by international law*" on the basis of a preliminary report submitted by the Special Rapporteur. He pointed out that the distinguishing feature of this topic is that its essential concern is with dangers that arise within the jurisdiction of one State and cause harmful effects beyond the borders of that State. It would appear from the Commission's discussion<sup>24</sup> that the acts or activities from which such dangers arise or which cause such harmful effects may be carried out by, *inter alia*, natural and juridical persons, including "transnational corporations", and may be activities having a trading or commercial aspect. Taking into account resolution 35/163, the Commission will continue its work on the topic and may have before it during its present session proposed draft articles which the Special Rapporteur intends to include in his next report.

26. In 1974, the Commission formulated a questionnaire to be communicated to Member States concerning the law of the non-navigational uses of international watercourses. Among the questions was one setting forth an outline of fresh water uses suggested as the basis for the Commission's study of the topic. That outline included the following: "(a) Agricultural uses: 1. Irrigation; 2. Drainage; 3. Waste disposal; 4. Aquatic food production. (b) Economic and commercial uses: 1. Energy production (hydroelectric, nuclear and mechanical); 2. Manufacturing; 3. Construction; 4. Transportation other than navigation; 5. Timber floating; 6. Waste disposal; 7. Extractive (mining, oil production, etc.)."<sup>25</sup> In provisionally adopting six draft articles on the topic at its 1980 session, the Commission noted that, at a future stage in its work, after having elaborated general principles relating to the non-navigational uses of international watercourse systems and their waters, it intends to examine the advisability of formulating, within the framework of the draft, additional draft articles on specific uses of international watercourse systems and their waters, such as those mentioned in its 1974 questionnaire, as well as on various measures of conservation related to such uses (and abuses such as pollution).<sup>26</sup> With regard to "agreements in the field of natural resources" the Commission and its Special Rapporteur in work on this topic have taken into account treaties considered relevant to the law of the non-navigational uses of international watercourses.<sup>27</sup> In addition, one article provisionally adopted in 1980 (article 5) concerned "Use of waters which constitute a shared natural resources".<sup>28</sup> Resolution 36/163 recommends that the Commission proceed with the preparation of draft articles on this topic, taking into account the replies to the questionnaire addressed to Governments.

27. The Commission also at its 1980 session provisionally adopted two draft articles on the topic of *jurisdictional immunities of States and their property*, one entitled "Scope of the present articles", the other "State immunity".<sup>29</sup> The Commission has not directly addressed itself as yet to such questions as the trading or commercial activities of a State which may be considered relevant to the topic, although the Special Rapporteur did allude to such questions in his second report.<sup>30</sup> He had proposed in that report a definition of "trading or commercial activity" as well as an interpretative provision for determining the "commercial character of a trading or commercial activity" but the Commission considered it premature at that stage to discuss the substance of definitional problems.<sup>31</sup> The Commission also noted that controversies had existed in the past concerning the divisibility of the functions of the State or the various distinctions between the activities carried on by modern States in fields of activity formerly undertaken

by individuals, such as trade and finance. The greatest care was called for in the treatment of this particular area of the topic.<sup>32</sup> In 1979 and 1980, the Legal Counsel of the United Nations circulated to Member States a questionnaire on the topic drafted by the Special Rapporteur in co-operation with the Secretariat. Included in the questionnaire were the following questions:

"Question 6. Do the laws and regulations . . . or the judicial practice . . . make any distinction, as far as jurisdictional immunities of foreign States and their property are concerned, between 'public acts' and 'non-public acts' of foreign States? . . .

"Question 7. If the answer to question 6 is 'yes':

" . . .

"(b) In a dispute relating to a contract of purchase of goods would courts of your State be expected to grant immunity to a foreign State which establishes that the ultimate object of the contract for a public purpose or the contract was concluded in the exercise of a 'public' or 'sovereign' function?

"(c) In a dispute relating to a foreign State's breach of a contract of sale, would courts of your State be expected to grant immunity to a foreign State which establishes that its conduct was motivated by public interests?

"(d) In any dispute concerning a commercial transaction, is the nature of transaction decisive of the question of State immunity, if not, how far is ulterior motive relevant to the question?

" . . .

"Question 12. What is the status, under laws and regulations in force or in practice in your State, of ships owned or operated by a foreign State and employed in commercial service?"

The text of the questionnaire and Government replies thereto, as well as of other information and materials relevant to the topic submitted by Governments, are presently before the Commission.<sup>33</sup> In addition, the Commission in 1980 "noted the special nature of the topic . . . which, more than other topics hitherto studied by it, touched on the realm of international law as well as that of private international law".<sup>34</sup> At its current session, it has before it a third report submitted by the Special Rapporteur containing five articles entitled as follows: Rules of competence and jurisdictional immunity; Consent of State; Voluntary submission; Counter-claims; and Waiver.<sup>35</sup> In connexion with the question of "rules of competence and jurisdictional immunity", the Special Rapporteur in that report included a section entitled "The rules of competence in private international law". The Commission intends as recommended by resolution 35/163 to proceed with the preparation of draft articles on the topic, taking into account replies to the questionnaire addressed to Governments as well as information furnished by them.

[A/CN.9/202/Add.4\*]

### Current activities of the European communities in the field of international trade law

The information on the current activities in the field of international trade law provided by the Commission of the European Communities (CEC) is contained in this addendum.

\* 1 July 1981.

<sup>32</sup> *Ibid.*, p. 321, para. 116.

<sup>33</sup> A/CN.4/343 and Add.1-3.

<sup>34</sup> *Official Records of the General Assembly, Thirty-fifth Session, Supplement No. 10 (A/35/10)*.

<sup>35</sup> A/CN.4/340 and Add.1.

<sup>24</sup> See *Official Records of the General Assembly, Thirty-fifth Session, Supplement No. 10 (A/35/10)*, chapter VII.

<sup>25</sup> *Ibid.*, p. 240, chapter V, para. 69.

<sup>26</sup> *Ibid.*, p. 250, para. 98.

<sup>27</sup> See the commentaries to articles 1, 3, 4 and 5, *ibid.*, chapter V.B.

<sup>28</sup> *Ibid.*, pp. 275-276.

<sup>29</sup> *Ibid.*, pp. 326, 328, chapter VI.B.

<sup>30</sup> A/CN.4/311 and Add.1.

<sup>31</sup> *Official Records of the General Assembly, Thirty-fifth Session, Supplement No. 10 (A/35/10)*, pp. 324-326, paras. 120, 122.

For completeness of the report of the Secretary-General contained in A/CN.9/202 and Add.1-3, this addendum is issued though the meeting of the fourteenth session, which was held from 19 to 26 June 1981, has taken place.

## PRIVATE INTERNATIONAL LAW<sup>1</sup>

### A. *International contracts*

1. The convention establishing uniform rules of conflict of laws in relation to contractual obligations has been signed by eight Member States. Four of these are already in the process of being ratified. Signature by the United Kingdom is expected to take place soon. Greece is considering the matter.

### B. *International payments*

2. Work in the field of guarantees and indemnities has been discontinued.

3. Consultation with Member States on reservation of title has proceeded apace. The Commission of the European Communities (CEC) expects to produce during the coming months a further draft proposal for a directive on simple reservation of title. CEC is collaborating very closely with the Council of Europe in this work.<sup>2</sup>

## PRODUCTS LIABILITY<sup>3</sup>

4. CEC submitted to the Council of the European Communities (EC) a proposal for a directive to harmonize the rules of law on the producer's liability for defective products. The text contemplates strict liability where the defective product causes personal injury or damage to property which is in private use.

## OTHER TOPICS OF INTERNATIONAL LAW<sup>4</sup>

### A. *Commercial agents*

5. CEC submitted to the Council of EC in January 1979 an amended proposal on the harmonization of the

laws of the Member States of EC relating to contract of commercial agency.

### B. *Company law*

6. CEC submitted an amended proposal for a Regulation on the Statute for European Companies to the Council of EC in 1975 (Bulletin of the EC Supplement 4/75). The Regulation's uniform legal framework would allow companies established under the various laws of the Member States of EC to reorganize themselves (by merger or the creation of holding companies or joint subsidiaries) at Community level. Being a complete new body of company law, the Statute includes rules on employee representation in the European Company. The proposal is at present under discussion in the Council of EC.

7. CEC submitted an amended proposal for a Regulation on the European Co-operation Grouping to the Council of EC in 1978 (O.J. No. C 103 of 28 April 1978). The Regulation would enable co-operation to take place between undertakings (particularly small and medium-sized) established under the various laws of the Member States of EC. It has yet to be discussed within the Council of EC.

8. The competent department of CEC is finalizing the text of a draft proposal for a directive to co-ordinate national laws relating to links between undertakings and particularly to groups. No text has yet been submitted to CEC for approval.

9. CEC's proposal for a First Council Directive on co-ordination of safeguards which are required concerning disclosure, the validity of obligations and the nullity of companies was adopted on 9 March 1968 (O.J. No. L 65 of 14 March 1968).

10. CEC's proposal for a Second Council Directive on co-ordination of safeguards required in respect of the formation of public limited liability companies and the maintenance and alteration of their capital was adopted on 13 December 1976 (O.J. No. L 26 of 31 January 1977).

11. CEC's proposal for a Third Council Directive concerning mergers of public limited liability companies was adopted on 9 October 1978 (O.J. No. L 295 of 20 October 1978).

12. CEC's proposal for a Fourth Council Directive on the annual accounts of limited liability companies was adopted on 25 July 1978 (O.J. No. L 222 of 14 August 1978).

13. CEC has made a proposal for a Fifth Council Directive on the structure of public limited liability companies and the powers and obligations of their organs (O.J. No. C 131 of 13 December 1972). It has also published a consultative document dealing with some of

<sup>1</sup> See A/CN.9/202/Add.2, XI. PRIVATE INTERNATIONAL LAW.

<sup>2</sup> *Ibid.*, XII. OTHER TOPICS OF INTERNATIONAL LAW, D. *Rights of Creditors*, para. 104.

<sup>3</sup> *Ibid.*, X. PRODUCTS LIABILITY.

<sup>4</sup> *Ibid.*, XII. OTHER TOPICS OF INTERNATIONAL LAW.

the issues raised by its proposal and entitled "Employee Participation and Company Structure in the European Community" (Bulletin of the EC Supplement 8/75). The proposal is at present before the Legal Affairs Committee of the European Parliament.

14. CEC has made an amended proposal for a Seventh Council Directive on consolidated accounts (O.J. No. C 14 of 17 January 1979). It is at present under discussion in the Council of EC.

15. CEC has made an amended proposal for an Eighth Council Directive on the authorization of persons responsible for carrying out statutory audits (O.J. No. C 317 of 18 December 1979). It is at present under discussion in the Council of EC.

16. CEC has prepared a Draft Convention on the international mergers of public limited liability companies (Bulletin of the EC Supplement 13/73). It is at present being discussed by the Member States of EC.

### C. Trade marks

17. CEC has made a proposal for a Council Directive to approximate the laws of the Member States relating to trade marks, and a proposal for a Council Regulation on the Community trade mark. These have been discussed by the Economic and Social Committee and have been laid before the European Parliament for debate.

## B. Report of the Secretary-General: question of co-ordination: direction of the work of the Commission (A/CN.9/203)\*

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\* 13 May 1981. Referred to in Report, paras. 39, 88 (part one, A, above).

## INTRODUCTION

1. The General Assembly in resolution 2205 (XXI),\* by which the United Nations Commission on International Trade Law was established, gave the Commission the mandate to co-ordinate legal activities in the field of the unification and harmonization of international trade law. This mandate was recently re-affirmed in resolutions 34/142\*\* of 17 December 1979 and 35/51\*\*\* of 4 December 1980.

2. In paragraph 5 (b) of resolution 34/142 the General Assembly requested the Secretary-General to place before the Commission, at each of its sessions, a report on the legal activities of the international organs, bodies and organizations concerned, together with recommendations as to steps to be taken by the Commission to fulfil its mandate. At this session the Commission will have before it a report on the work of other organizations engaged in the field of international trade law.<sup>1</sup>

3. The Secretariat was of the view that it might be an appropriate time to set out the various approaches taken by the Commission in fulfilling its mandate given by the General Assembly. Accordingly, the present report in part two describes in brief the work undertaken by the Commission, emphasizing, however, the role of co-ordination in that work. It was believed that the Commission would be able to engage in meaningful consideration on the question of co-ordination with this information available. Part one describes the mandate of the Commission as the central organ in the United Nations for the unification and harmonization of international trade law. Part three discusses relevant questions of methodology.

## PART I. THE MANDATE OF THE COMMISSION

4. During the consideration by the Sixth Committee of the draft resolution which eventually was adopted as resolution 2205 (XXI) it was recognized that a large number of organizations and bodies both within and without the United Nations were already engaged in formulating texts on international trade law.<sup>2</sup> In some

cases these formulating agencies were restricted to a particular subject matter, such as maritime law in the case of the Inter-Governmental Maritime Consultative Organization. Other formulating agencies which had a broader subject matter competence did not command world-wide acceptance. They did not have balanced representation of countries of market economy and of centrally planned economy, or of countries with developed and developing economies. In some cases, those agencies had a membership confined either to countries of centrally planned economy (e.g. the Council for Mutual Economic Assistance (CMEA)) or to participants from countries of market economy (e.g. the International Chamber of Commerce (ICC)); in other instances, members came only from a specific region (e.g. the Economic Commission for Europe (ECE)). In the case of the International Institute for the Unification of Private Law (UNIDROIT), although there was no geographical limitation on membership, the membership was predominantly European.

5. Experience showed that texts were seldom adopted by countries which had not participated in the work of a particular formulating agency, and too often were not adopted even by those countries which had participated in the work. There was a great disproportion between the number of draft instruments prepared by formulating agencies and their acceptance by States. Moreover, the lack of co-ordination among the formulating agencies led to the elaboration of texts on similar subjects with inconsistent rules. The result was a duplication of effort and confusion as to the law applicable to particular transactions.

6. It was expected that a commission of the United Nations specifically concerned with the harmonization and unification of international trade law would improve the situation. The Commission would have a broad competence as to subject matter and its membership would consist of States from the various legal, economic and social systems making the results of its work more acceptable throughout the world.

7. It was not expected that the work of the new commission would reduce the usefulness of the existing formulating agencies. Rather, it was expected that United Nations' interest and participation in this work through the new commission would tend to broaden the scope of the existing agencies and enhance their activities. Texts which had been formulated and were already in use within a region or among certain States might be recommended for use on a global level. In some cases, the Commission might recommend to a formulating agency that it undertake certain work because of its acknowledged expertise. In other cases, the Commission might be requested by a formulating agency to undertake the work itself because it would be a more appropriate forum for the particular problem.

\* Yearbook . . . 1968-1970, part one, II, E.

\*\* Yearbook . . . 1980, part one, I, C.

\*\*\* Yearbook . . . 1980, part one, II, D.

<sup>1</sup> A/CN.9/202 and Add.1 and 2 (reproduced in this volume, part two, V, A). See also Report of the United Nations Commission on International Trade Law on the work of its thirteenth session, *Official Records of the General Assembly, Thirty-fifth Session, Supplement No. 17 (A/35/17)*, para. 150 (Yearbook . . . 1980, part one, II, A).

<sup>2</sup> The discussion in part one is a summary of the Report of the Secretary-General, "Progressive development of the law of international trade", *Official Records of the General Assembly, Twenty-first Session, Annexes*, agenda item 88, (A/6396), paras. 208-234 (Yearbook . . . 1968-1970, part one, II, B).



8. With these considerations in mind, the General Assembly indicated a wide range of activities to be undertaken by the Commission in fulfilling its mandate to "further the progressive harmonization and unification of the law of international trade". In resolution 2205 (XXI), Section II, para. 8, the Commission, in addition to preparing new international conventions, model laws and uniform law, was called on to:

(a) Co-ordinate the work of organizations active in this field;

(b) Encourage co-operation among them;

(c) Promote wider participation in existing international conventions;

(d) Promote wider acceptance of existing model and uniform laws;

(e) Promote the adoption of new international conventions and model and uniform laws;

(f) Promote the codification and wider acceptance of international trade terms, provisions, customs and practices;

(g) Promote ways and means of ensuring a uniform interpretation and application of international conventions and uniform laws in the field of international trade law;

(h) Collect and disseminate information on national legislation and modern legal developments, including case law, in the field of the law of international trade.

## PART II. ACTIONS TAKEN BY THE COMMISSION

9. The report of the first session of the Commission shows that

"There was general recognition that the establishment of the Commission marked the opening of a new and important chapter in the progressive harmonization and unification of the law of international trade. The Commission, whose membership reflected the principal economic and legal systems of the world and the developed and developing countries, was considered to be most suited for the purpose of eliminating divergencies between national systems of law which formed barriers to the development of international trade. While the work facing the Commission was considerable, both in scope and complexity, there were a number of encouraging factors. The unanimous adoption by the General Assembly of resolution 2205 (XXI), which established the Commission, augured well for the work of harmonization and unification. The hope was expressed, by a number of representatives, that out of the co-operative endeavours of the Commission and of other bodies active in the field, a

new *lex mercatoria* would in time evolve reflecting the interest of the entire international community."<sup>3</sup>

10. The co-operative endeavours of the Commission to bring about the harmonization and unification of international trade law fall into two major divisions. The first has to do with the elaboration and promotion of specific texts dealing with international trade law. The second involves a programme of information and publication to disseminate knowledge of the current status of international trade law. These two major divisions of the work will be dealt with in turn.

### A. Elaboration and promotion of texts

11. Although the General Assembly had given the Commission the mandate to promote the harmonization and unification of international trade law and had authorized it to employ a number of different techniques to fulfil that mandate, it was up to the Commission itself to decide on the manner in which it would proceed. At the one extreme the Commission could have turned its attention exclusively to the preparation of new texts in fields where no text existed at a universal level or to the revision of existing texts which were considered to be out of date. On the other hand the Commission could have considered itself to be a policy making body, leaving the preparation of legal texts to other formulating agencies. The most ambitious proposal of this nature was put forward by the delegation of France.

"Rather than actually drafting texts, UNCITRAL would have the task of approving texts drafted elsewhere, although perhaps on UNCITRAL's initiative and its suggestion . . .

"The regulations approved by UNCITRAL could, of course, be highly varied in form and substance. Sometimes it would approve actual laws with specific detailed provisions; sometimes it would approve mere principles for States to apply; and sometimes it would simply be a matter of definitions to elucidate the meaning and scope of various terms. Every kind of formula can be utilized in reconstituting a common body of law."<sup>4</sup>

12. The French proposal was not adopted. However, the basic idea it reflected has been followed by the Commission. A significant element in the contribution of the Commission to the harmonization and unification of international trade law has been the endorsement of texts developed by other organizations. Moreover, these texts, as well as those prepared by the Commission itself, have been "highly varied in form and substance".

<sup>3</sup> Official Records of the General Assembly, Twenty-third Session, Supplement No. 16 (A/7216), para. 22 (Yearbook . . . 1968-1970, part two, I, A).

<sup>4</sup> Draft basic convention establishing a common body of international trade law, UNCITRAL/III/CRP.3, para. 8 (Yearbook . . . 1968-1970, part three, V, B).



# 1. Promotion of texts of other formulating agencies

## (a) Urged ratification of United Nations convention

13. The Commission has promoted the ratification of a convention adopted by the United Nations under other auspices, having recommended at its second, third, sixth and twelfth sessions that States which have not ratified or acceded to the 1958 United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards should do so.<sup>5</sup> On the recommendation of the Commission, the General Assembly has also urged ratification or accession by those States which had not yet done so.<sup>6</sup> Furthermore, the Commission at its tenth session welcomed the resolution of the Asian-African Legal Consultative Committee that those States in the Asian-African region which had not yet ratified or acceded to the Convention consider doing so.<sup>7</sup>

## (b) Urged ratification of regional convention

14. The Commission, at its sixth session, promoted the ratification of a convention adopted at a regional level when it invited "the Economic Commission for Europe to draw the attention of the States which are eligible to ratify or accede to the 1961 European Convention on International Commercial Arbitration but have not done so, to the existence of that Convention and to invite them to indicate whether they intend to adhere thereto".<sup>8</sup>

## (c) Recommended use of trade terms and contract provisions

15. The Commission has twice recommended the use on a world-wide basis of model trade terms or contract provisions. At its second session it urged the International Chamber of Commerce "to give the widest possible dissemination to Incoterms 1953 in order to encourage their world-wide use in international trade".<sup>9</sup> It also commended, at its eighth session, the use of 1974 revision of Uniform Customs and Practice for Documentary Credits in transactions involving the establishment of a documentary credit.<sup>10</sup>

<sup>5</sup> *Official Records of the General Assembly, Twenty-fourth Session, Supplement No. 18 (A/7618)*, para. 112 (Yearbook . . . 1968-1970, part two, II, A); *ibid.*, *Twenty-fifth Session, Supplement No. 17 (A/8017)*, para. 156 (Yearbook . . . 1968-1970, part two, III, A); *ibid.*, *Twenty-eighth Session, Supplement No. 17 (A/9017)*, para. 85 (Yearbook . . . 1973, part one, II, A); *ibid.*, *Thirty-fourth Session, Supplement No. 17 (A/34/17)*, para. 81 (Yearbook . . . 1979, part one, II, A).

<sup>6</sup> Resolution 3108 (XXVIII) of 12 December 1973, para. 5 (Yearbook . . . 1974, part one, I, C).

<sup>7</sup> *Official Records of the General Assembly, Thirty-second Session, Supplement No. 17 (A/32/17)*, para. 39 (Yearbook . . . 1977, part one, II, A).

<sup>8</sup> *Ibid.*, *Twenty-eighth Session, Supplement No. 17 (A/9017)*, para. 85 (Yearbook . . . 1973, part one, II, A).

<sup>9</sup> *Ibid.*, *Twenty-fourth Session, Supplement No. 18 (A/7618)*, para. 60 (Yearbook . . . 1968-1970, part two, II, A).

<sup>10</sup> *Ibid.*, *Thirtieth Session, Supplement No. 17 (A/10017)*, para. 41 (Yearbook . . . 1975, part one, II, A).

## (d) Transmitted general conditions to regional organizations

16. The Commission has twice transmitted to the regional organizations sets of general conditions produced in other regions for their consideration. The text of the ECE general conditions relating to plant, machinery, engineering goods and lumber were transmitted by the Commission at its second session to the other regional economic commissions, as well as to other regional organizations active in the field of international trade law, with a request that they consult the Governments of the respective regions and/or interested trade circles for the purpose of obtaining their views and comments on the desirability of extending the use of those general conditions to the regions concerned.<sup>11</sup> In addition, the Commission requested the Secretary-General to transmit to the regional economic commissions for their use in the development of general conditions on a regional basis the text in English, French, Russian and Spanish of the General Conditions of Delivery (1968) of the Council for Mutual Economic Assistance.<sup>12</sup>

# 2. Requests to other formulating agencies to undertake work

## (a) Contract guarantees

17. The Commission at its third session noted that the ICC had begun work towards the preparation of rules in respect of tender guarantees, performance guarantees and repayment guarantees. Several representatives suggested that the ICC's study should be expanded to include payment guarantees. In order to secure the views of banking and trade institutions in countries not represented in ICC, the Commission requested the Secretary-General to address a questionnaire on the subject to Governments and also to banking and trade institutions in countries not represented in ICC and to transmit to it the observations received. The Commission also requested the ICC to submit to it reports on the progress made by it and its proposed action in the matter of bank guarantees.<sup>13</sup>

18. The observations received by the Secretary-General were forwarded to the ICC for its use. Pursuant to the request of the Commission, ICC submitted reports to the fourth, seventh, eighth and tenth sessions of the Commission.

19. At its tenth session, the Commission decided to review the item of contract guarantees at its eleventh session.<sup>14</sup> Although the ICC adopted its Uniform Rules

<sup>11</sup> *Ibid.*, *Twenty-fourth Session, Supplement No. 18 (A/7618)*, para. 60 (Yearbook . . . 1968-1970, part two, II, A).

<sup>12</sup> *Ibid.*

<sup>13</sup> *Official Records of the General Assembly, Twenty-fifth Session, Supplement No. 17 (A/8017)*, paras. 130-138 (Yearbook . . . 1968-1970, part two, III, A).

<sup>14</sup> *Ibid.*, *Thirty-second Session, Supplement No. 17 (A/32/17)*, para. 38 (Yearbook . . . 1977, part one, II, A).

on Contract Guarantees (ICC publication No. 325) in 1978, the Commission has not had the occasion to review the subject.

20. The Commission at its twelfth session noted that the work of the ICC in respect of documentary letters of credit and contract guarantees had a direct bearing on work in respect of stand-by letters of credit.<sup>15</sup>

(b) *Stand-by letters of credit*

21. At its eleventh session, the Commission included, as a priority topic in its new programme of work, the item entitled "Stand-by letters of credit" and requested the Secretariat to study this topic in conjunction with ICC.<sup>16</sup> At its twelfth session the Commission received a report from the Secretary-General which reviewed the work being done by ICC.<sup>17</sup> The Commission requested the ICC to continue its work on stand-by letters of credit and to submit to it the results of its work before final adoption by its competent organs.<sup>18</sup>

22. ICC is currently considering the possibility of incorporating in a new revision of the 1974 version of Uniform Customs and Practice for Documentary Credits specific provisions dealing with stand-by letters of credit. At the request of ICC the Secretariat of the Commission sent a note verbale to Governments enclosing a questionnaire prepared by ICC which inquires, *inter alia*, as to the use of Uniform Customs and Practice in connexion with stand-by letters of credit.

(c) *Hague Convention of 1955 on conflict of laws in sales*

23. The Commission, at its first session, decided to send a questionnaire to States members of the United Nations and States members of any of its specialized agencies as to whether they intended to adhere to the 1955 Hague Convention on the Law Applicable to International Sales of Goods and the reasons for their positions.<sup>19</sup> At its second session the Commission referred the Convention and the replies received to the Working Group on the International Sale of Goods.<sup>20</sup> The Working Group, however, concentrated its efforts on the revision of the two Hague Conventions of 1964, discussed below.

24. The Commission, at its eleventh session, decided to retain the 1955 Hague Convention on its programme

of work and indicated it was "to be considered only after the Hague Conference on Private International Law had completed its revision of that Convention".<sup>21</sup>

25. The Hague Conference on Private International Law, at its fourteenth session, decided "to include with priority in the Agenda of the Conference the revision of the Convention of June 15, 1955 on the law applicable to international sales of goods".<sup>22</sup>

(d) *Geneva Convention of 1930 on conflict of laws in negotiable instruments*

26. At the fourth session of the Working Group on International Negotiable Instruments it was noted that, by virtue of articles 9 and 10 of the Geneva Convention of 1930 for the Settlement of Certain Conflicts of Laws in connexion with Bills of Exchange and Promissory Notes, States having ratified that Convention might be prevented from ratifying a convention on international bills of exchange and international promissory notes, as was being prepared by the Working Group.<sup>23</sup> Several possible solutions were suggested, among which was the fact that the Hague Conference on Private International Law had included the question of conflicts of law in the field of negotiable instruments in its programme of work and was considering the possibility of a revision of the Geneva Convention of 1930 or of drawing up a new convention on conflicts of law in this field. The Working Group decided to return to the question at its fifth session.

27. At its fifth session the Working Group suggested that the Hague Conference might wish to give priority to the consideration of the relationship between the 1930 Geneva Convention on conflicts of law and the draft Convention being prepared by the Working Group.<sup>24</sup>

28. The Hague Conference, at its fourteenth session (1980), decided to take under consideration the preparation of a convention on the law applicable to negotiable instruments as a subject to be included in the agenda of a future session.<sup>25</sup> The Conference decided to leave to the Secretary-General of the Conference the responsibility of apprising the Governments of the Member States of the Conference of a proposal to initiate work at an inter-governmental level when, having particular regard to the advanced progress of the work undertaken within UNCITRAL, the time appears appropriate.

(e) *Participation by non-member States in work of other formulating agencies*

29. A recommendation by the Commission that an organ with less than universal membership undertake

<sup>15</sup> *Ibid.*, Thirty-fourth Session, Supplement No. 17 (A/34/17), para. 48 (Yearbook . . . 1979, part one, II, A).

<sup>16</sup> *Ibid.*, Thirty-third Session, Supplement No. 17 (A/33/17), para. 67 (Yearbook . . . 1978, part one, II, A).

<sup>17</sup> A/CN.9/163 (Yearbook . . . 1979, part two, II, B).

<sup>18</sup> *Official Records of the General Assembly, Thirty-fourth Session, Supplement No. 17 (A/34/17)*, para. 48 (Yearbook . . . 1979, part one, II, A).

<sup>19</sup> *Official Records of the General Assembly, Twenty-third Session, Supplement No. 16 (A/7216)*, para. 48, subpara. 17 (Yearbook . . . 1968-1970, part two, I, A).

<sup>20</sup> *Ibid.*, Twenty-fourth Session, Supplement No. 18 (A/7618), para. 38 (Yearbook . . . 1968-1970, part two, II, A).

<sup>21</sup> *Ibid.*, Thirty-third Session, Supplement No. 17 (A/33/17), para. 67 (Yearbook . . . 1978, part one, II, A).

<sup>22</sup> Final Act, E.1.a.

<sup>23</sup> A/CN.9/117, paras. 64-65 (Yearbook . . . 1976, part two, II, 1).

<sup>24</sup> A/CN.9/141, para. 15 (Yearbook . . . 1978, part two, II, A).

<sup>25</sup> Final Act, E.2.a.

work in the field of international trade law of a nature to be of universal concern raises problems concerning the participation of States which are not members of the organ concerned.

30. ICC. The problem was first considered at the Commission's third session in connexion with the contemplated revision of the Uniform Customs and Practice for Documentary Credits by the International Chamber of Commerce.<sup>26</sup> The Commission welcomed the work of revision of the 1962 version scheduled to be undertaken by the ICC. At the same time, it felt that, in view of the widespread use of Uniform Customs (1962), a procedure should be developed that would permit interested circles in countries not represented in the ICC to make observations on the operation of Uniform Customs (1962), so that these could be taken into account by the ICC. The Commission was agreed that the Secretary-General should be requested to invite Governments and banking and trade institutions to submit such observations as they might wish to make on Uniform Customs (1962) for transmission to the ICC.

31. The Secretary-General received replies from 42 Governments and nine replies from banking and trade institutions.<sup>27</sup> These replies were transmitted to the ICC for consideration. They were also analysed and presented to the Commission for its use when the Commission decided to commend the use of the 1974 version of Uniform Customs and Practice.

32. The procedure by which the Secretary-General has sent to Governments a questionnaire prepared by the ICC in order to solicit the views of States not represented in it by a national committee is now well established, having been used in respect of contract guarantees as well as in the currently contemplated revision of the 1974 version of Uniform Customs and Practice for Documentary Credits.

33. *Hague Conference.* At its thirteenth session, the Commission was informed that it was intended to request the Fourteenth Session of the Hague Conference on Private International Law to change the procedures of the Conference so that, when it was dealing with matters of universal interest, such as matters of international trade law, all States would be invited to participate.<sup>28</sup>

34. The Hague Conference, at its fourteenth session (1980), adopted the following decision:

"Having regard to the discussions which took place within the Fourth Commission on the desirability of

admitting the participation of non-member States in the work of the Conference where the subject-matter—such as the law of international trade—lends itself thereto;

"Considering that such a policy would be of a nature to increase respect for the area of activity of the Conference by other international organizations, in particular the United Nations Commission on International Trade Law (UNCITRAL);

"Grants that non-Member States may participate in the work of the Conference where, by virtue of the subject treated, it is felt that such participation is necessary;

"Decides that the implementation of this principle will be the subject, in each particular case, of a decision of the Governments of the Member States taken at a Plenary Session or within a Special Commission on general matters and policy of the Conference."<sup>29</sup>

35. At the same time it decided that this principle should be applied in respect of the revision of the 1955 Convention on the Law Applicable to International Sales of Goods<sup>30</sup> and left it to the Secretary-General of the Conference to decide on the application of this principle in the preparation of an eventual convention on the law applicable to negotiable instruments.<sup>31</sup>

### 3. *Revision of work done by other agencies*

#### (a) *Hague Conventions of 1964 on sales*

36. The Commission at its first session decided to send a questionnaire to States members of the United Nations and States members of any of its specialized agencies as to whether they intended to adhere to the 1964 Hague Convention relating to a Uniform Law on the International Sale of Goods and to the 1964 Hague Convention relating to a Uniform Law on the Formation of Contracts for the International Sale of Goods and their reasons for their positions.<sup>32</sup> The Commission, after reviewing the analysis of replies at its second session, decided to create a Working Group on the International Sale of Goods to ascertain which modifications of the existing texts might render them capable of wider acceptance by countries of different legal, social and economic systems.<sup>33</sup>

37. The result of the work undertaken by the Working Group is the United Nations Convention on Con-

<sup>26</sup> *Official Records of the General Assembly, Twenty-fifth Session, Supplement No. 17 (A/8017)*, paras. 119-125 (Yearbook . . . 1968-1970, part two, III, A).

<sup>27</sup> A/CN.9/101, para. 1 (Yearbook . . . 1975, part two, II, 3). The analysis of replies is to be found in A/CN.9/101/Add.1 (*ibid.*, part two, II, 4).

<sup>28</sup> *Official Records of the General Assembly, Thirty-fifth Session, Supplement No. 17 (A/35/17)*, para. 148 (Yearbook . . . 1980, part one, II, A).

<sup>29</sup> Final Act, D.1.

<sup>30</sup> *Ibid.*, E.1.b.

<sup>31</sup> Final Act, E.2.b.

<sup>32</sup> *Official Records of the General Assembly, Twenty-third Session, Supplement No. 16*, para. 48 sub-para. 14 (Yearbook . . . 1968-1970, part two I, A).

<sup>33</sup> *Ibid.*, Twenty-fourth Session, Supplement No. 18 (A/7618), para. 38 (Yearbook . . . 1968-1970, part two, II, A).

tracts for the International Sale of Goods, adopted on 10 April 1980 at Vienna.<sup>34</sup>

(b) *Brussels Convention of 1924 on bills of lading*

38. At its fourth session the Commission decided to examine the International Convention for the Unification of Certain Rules relating to Bills of Lading (the Brussels Convention of 1924) and the Protocol to amend that Convention (the Brussels Protocol of 1968) with a view to revising and amplifying the rules as appropriate.<sup>35</sup> In this examination there was close co-operation between the Commission and the United Nations Conference on Trade and Development. The result of this examination was the United Nations Convention on the Carriage of Goods by Sea adopted on 31 March 1978 at Hamburg.<sup>36</sup>

(c) *New York Convention of 1958 on arbitration-model arbitration law*

39. The Commission, at its tenth session, considered certain recommendations of the Asian-African Legal Consultative Committee (AALCC) relating to international commercial arbitration.<sup>37</sup> These recommendations were aimed at ensuring the autonomy of parties to agree on arbitration rules irrespective of any contrary provision of the law applicable to the arbitration, at safeguarding fairness in arbitral proceedings, and at excluding reliance on sovereign immunity in international commercial arbitration.<sup>38</sup> It was suggested by AALCC that these issues could possibly be clarified in a protocol to the 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards.

40. In the decision taken at its tenth session the Commission requested the Secretary-General to consult with AALCC and other interested international organizations and to prepare studies on the matters raised by AALCC. Pursuant to this request the Secretary-General submitted two reports to the twelfth session of the Commission. One analysed over one hundred court decisions concerning the application and interpretation of the 1958 New York Convention.<sup>39</sup> The report concluded that the Convention, despite some minor deficiencies, had satisfactorily met the general purpose for which it was adopted.

41. The second was a note by the Secretariat which discussed the need for greater uniformity of national laws on arbitral procedure and the desirability of establishing standards for modern and fair arbitration pro-

cedures.<sup>40</sup> The note suggested that the Commission commence work on a model law on arbitral procedure which could help to overcome most of the problems identified in the above survey and meet the concerns expressed in the recommendations of AALCC.

42. The Commission agreed at its twelfth session that there was no need to alter or amend, by way of revision or protocol, the 1958 Convention.<sup>41</sup> At the same time it was agreed that a model law could assist States in reforming and modernizing their law on arbitration procedure and would thus help to reduce the divergencies encountered in the interpretation of the 1958 New York Convention.

43. At this session the Commission will have before it a report of the Secretary-General on the identification of issues possibly to be included in a model arbitration law.<sup>42</sup>

4. *Reliance upon existing texts as models*

44. In some cases the Commission has undertaken work in a field in which there was no existing international text of universal applicability to be adopted, approved or revised. In these cases the Commission has expected the Secretariat to rely upon the existing regional, national or private texts already in existence as models for its own. In some cases this expectation has been explicit in the decision by the Commission while in other cases the preparatory work by the Secretariat has made clear the sources which could be relied upon.

(a) *UNCITRAL Arbitration Rules*

45. The decision by the Commission at its sixth session to request the Secretary-General to prepare a draft set of arbitration rules for optional use in *ad hoc* arbitration relating to international trade<sup>43</sup> arose out of an original recommendation by the Special Rapporteur, Mr. Ion Nestor (Romania), that further study be given to the desirability of drawing up a model set of arbitration rules containing basic provisions.<sup>44</sup> It was noted in his report that there were innumerable sets of arbitration rules, almost all of which had been prepared for the use of a single arbitration centre, with no single set of arbitration rules serving as a model for the others. Nevertheless, it had been noted that "Even in the absence of evident harmony among the various provisions of the rules, the Economic Commission for Europe was able to deduce the general principles of those rules".<sup>45</sup> There-

<sup>34</sup> A/CONF.97/18, Annex I (Yearbook . . . 1980, part three, I, B).

<sup>35</sup> *Official Records of the General Assembly, Twenty-sixth Session, Supplement No. 17 (A/8417)*, para. 19 (Yearbook . . . 1971, part one, II, A).

<sup>36</sup> A/CONF.89/13, Annex I (Yearbook . . . 1978, part three, I, B).

<sup>37</sup> *Official Records of the General Assembly, Thirty-second Session, Supplement No. 17 (A/32/17)*, annex II, paras. 27-37 (Yearbook . . . 1977, part one, II, A, Annex II).

<sup>38</sup> The recommendations of AALCC are contained in A/CN.9/127, Annex (Yearbook . . . 1977, part two, III).

<sup>39</sup> A/CN.9/168 (Yearbook . . . 1979, part two, III, C).

<sup>40</sup> A/CN.9/169 (Yearbook . . . 1979, part two, III, D).

<sup>41</sup> *Official Records of the General Assembly, Thirty-fourth Session, Supplement No. 17 (A/34/17)*, paras. 76-81 (Yearbook . . . 1979, part one, II, A).

<sup>42</sup> A/CN.9/207 (reproduced in this volume, part two, III).

<sup>43</sup> *Official Records of the General Assembly, Twenty-eighth Session, Supplement No. 17 (A/9017)*, para. 85 (Yearbook . . . 1973, part one, II, A).

<sup>44</sup> A/CN.9/64, para. 180 (Yearbook . . . 1972, part two, III).

<sup>45</sup> *Ibid.*, para. 178.

fore, it was thought possible to draw up model rules containing basic provisions which would subsequently be recommended to all arbitration centres for gradual inclusion in their rules.

46. The Secretary-General in presenting the analysis of the comments of Governments on the proposals of the Special Rapporteur noted that there were two existing sets of arbitration rules drawn up by regional economic commissions: the Arbitration Rules of the Economic Commission for Europe (ECE Rules), adopted in 1966, and the Rules for International Commercial Arbitration of the United Nations Economic Commission for Asia and the Far East (ECAFE Rules), adopted in 1966.<sup>46</sup>

47. The Secretary-General suggested that in view of the experience gained in respect of those regional uniform rules, the Commission might wish to consider whether the drawing up of a set of arbitration rules for world-wide use in *ad hoc* arbitration would not be the most appropriate method for the realization of the Special Rapporteur's proposal. He suggested that such a set of rules could immediately be used, if chosen by the parties, in *ad hoc* arbitration. In addition, such uniform rules for *ad hoc* arbitration might be found useful if it were decided at a later stage to give further attention to the harmonization of the rules of existing arbitration centres. Thus, such uniform rules could, even before their acceptance by existing arbitration centres, contribute to the unification of commercial arbitration, not only in those regions where uniform rules and appropriate arbitration centres already existed but also in other countries and regions and in international trade.

48. In preparing the draft Rules, the Secretary-General, at the request of the Commission, took into account the ECE Rules and the ECAFE Rules. He also took into account the following rules: the Rules of Conciliation and Arbitration of the International Chamber of Commerce, 1975, the Rules of Procedure of the Inter-American Commercial Arbitration Commission, the Commercial Arbitration Rules of the American Arbitration Association, the Rules of Procedure of the Foreign Trade Arbitration Commission at the USSR Chamber of Commerce. In addition, he took account of three conventions: the Convention on the Recognition and Enforcement of Foreign Arbitral Awards, New York, 1958, the European Convention on International Commercial Arbitration, Geneva, 1961, and the Convention on the Settlement of Investment Disputes between States and Nationals of Other States, Washington, 1965.<sup>47</sup>

49. The Secretary-General prepared the draft Rules in consultation with the International Committee on Commercial Arbitration. At the request of the Commission, the Secretary-General, prior to presenting the

draft Rules to the Commission, circulated them for comments to the regional economic commissions of the United Nations and to centres of commercial arbitration, some 75 in total. In addition, the draft Rules were discussed at the Fifth International Arbitration Congress held at New Delhi, India, from 7 to 10 January 1975 prior to their consideration by the Commission.

50. The Commission adopted the UNCITRAL Arbitration Rules at its ninth session in 1976.<sup>48</sup>

#### (b) *UNCITRAL Conciliation Rules*

51. A similar approach was taken in the preparation of the UNCITRAL Conciliation Rules. In particular, in the preparation of the draft Rules, the Secretariat held consultations with representatives of the International Council for Commercial Arbitration and the International Chamber of Commerce. Prior to their consideration and adoption by the Commission at its thirteenth session, the draft Rules were transmitted to Governments and interested international organizations for their observations.<sup>49</sup>

#### (c) *UNIDROIT draft law on validity of contracts*

52. The Commission, at its sixth session, noted the receipt of a letter from the President of UNIDROIT which transmitted the text of a "draft of a law for the unification of certain rules relating to the validity of contracts of international sale of goods" and which invited the Commission to include the consideration of this draft as an item on its agenda.<sup>50</sup> At its seventh session the Commission requested the Working Group on the International Sale of Goods "after having completed its work on the uniform law on the international sale of goods, to consider the validity of contracts for the international sale of goods, on the basis of the . . . UNIDROIT draft, in connexion with its work on uniform rules governing the formation of contracts for the international sale of goods."<sup>51</sup>

53. The Working Group considered the draft law at its eighth and ninth sessions and decided that articles 3 to 5 on interpretation of statements by and acts of the parties should be included in the draft convention on formation of contracts for the international sale of goods. These articles, as amended, appear as article 8 of the United Nations Convention on Contracts for the International Sale of Goods.<sup>52</sup>

<sup>48</sup> Official Records of the General Assembly, Thirty-first Session, Supplement No. 17 (A/31/17), para. 56 (Yearbook . . . 1976, part one, II, A).

<sup>49</sup> Official Records of the General Assembly, Thirty-fifth Session, Supplement No. 17 (A/35/17), paras. 30 and 106 (Yearbook . . . 1980, part one, II, A).

<sup>50</sup> Ibid., Twenty-eighth Session, Supplement No. 17 (A/30/17), paras. 144-148 (Yearbook . . . 1973, part one, II, A).

<sup>51</sup> Ibid., Twenty-ninth Session, Supplement No. 17 (A/29/17), para. 93 (Yearbook . . . 1974, part one, II, A).

<sup>52</sup> A/CONF.97/18, Annex I (Yearbook . . . 1980, part three, I, B).

<sup>46</sup> A/CN.9/112, paras. 1-8 (Yearbook . . . 1976, part two, III, 1).

<sup>47</sup> A/CN.9/112, paras. 1-8 (Yearbook . . . 1976, part two, III, 1).

(d) *New York Convention of 1974 on limitations in sales*

54. When the Commission, at its second session, decided to create a Working Group on Time-Limits and Limitations (Prescription) and to request it to study the topic of time-limits and limitations (prescription) in the field of international sale of goods with a view to the preparation of a preliminary draft of an international convention, it had before it (1) the preliminary draft Convention on the proper law and unification of provisions concerning prescription in connexion with materialization of international trade, prepared in 1961 within the framework of the Council for Mutual Economic Assistance, (2) the provisions on prescription in the General Conditions of Delivery, 1968, of the Council for Mutual Economic Assistance, (3) a preliminary draft convention on the uniform effect of the lapse of time on international sales of tangible movables, prepared by Professor H. Trammer of Poland, and (4) draft European rules on extinctive prescription, prepared within the framework of the Council of Europe.<sup>53</sup>

55. The result of the work undertaken by the Working Group is the Convention on the Limitation Period in the International Sale of Goods, adopted on 12 June 1974 in New York.<sup>54</sup>

(e) *Draft convention on negotiable instruments*

56. The Commission, at its second session, considered the possibilities for the harmonization and unification of the law of negotiable instruments.<sup>55</sup> It noted that there were two principal systems of negotiable instruments law, i.e. that represented by the Geneva Conventions of 1930 and 1931 and that represented by the Bills of Exchange Act, 1882 of the United Kingdom (BEA) and the United States Uniform Commercial Code (UCC), even though within these systems complete unification had not yet been achieved.

57. The Commission was of the opinion that a parallel unification of the two main systems would be a difficult and long-term task and that the work of unification should be concentrated on creating a new negotiable instrument for international payments that would reduce the problems arising out of the two systems. Therefore, the draft Convention on International Bills of Exchange and International Promissory Notes, which has been prepared by the Working Group on International Payments, has been based on a synthesis of the 1930 Geneva Uniform Law on Bills of

Exchange and Promissory Notes, the BEA and the UCC.<sup>56</sup>

(f) *New international economic order: industrial contracts*

58. The Working Group on the New International Economic Order, at its session held in New York in January 1980, recommended to the Commission for possible inclusion in its work programme, *inter alia*:

"Harmonization, unification and review of contractual provisions commonly occurring in international contracts in the field of industrial development, such as contracts on research and development, consulting, engineering, supply and construction of large industrial works (including turn-key contracts or contracts *produit en main*), transfer of technology (including licensing), service and maintenance, technical assistance, leasing, joint venture, and industrial co-operation in general."<sup>57</sup>

59. The Working Group was of the opinion that this item would be of special importance to developing countries and to the work of the Commission in the context of the new international economic order.<sup>58</sup> The Group therefore requested the Secretariat to prepare a study on this item and submit it to the Commission at its next session so that the Commission could take its decisions in full knowledge of the issues involved.

60. The report submitted by the Secretariat discussed each of the ten types of contracts in the field of industrial development mentioned by the Working Group in terms of their main characteristics and contents, existing legislation, work done by other international organizations and bodies and possible work to be done by UNCITRAL.<sup>59</sup> In general, it was found that few countries had existing legislation directed specifically at any of these types of contracts, but that a number of international organizations, both public and private, had prepared model or standard contracts, checklists or guides for the negotiation of such contracts.

61. The Commission at its thirteenth session considered the report of the Secretary-General and decided to commence work on contractual provisions relating to contracts for the supply and construction of large industrial works (including turn-key contracts or contracts *produit en main*) and contracts on industrial co-opera-

<sup>56</sup> The original draft of a uniform law on international bills of exchange with commentary was in A/CN.9/67 (Yearbook . . . 1972, part two, II, 1). When it was decided to expand the proposed uniform law to include promissory notes, a new draft was prepared based on the same principles (A/CN.9/WG.IV/WP.2 (Yearbook . . . 1973, part two, II, 2)). It was the latter text which has formed the basis of deliberations of the Working Group.

<sup>57</sup> A/CN.9/176, para. 31 (Yearbook . . . 1980, part two, V, A).

<sup>58</sup> This recommendation was supported by the Asian-African Legal Consultative Committee, A/CN.9/194 (Yearbook . . . 1980, part two, V, D).

<sup>59</sup> A/CN.9/191 (Yearbook . . . 1980, part two, V, B).

<sup>53</sup> Official Records of the General Assembly, Twenty-fourth Session, Supplement No. 18 (A/7618), paras. 40-46 (Yearbook . . . 1968-1970, part two, II, A).

<sup>54</sup> A/CONF.63/15 (Yearbook . . . 1974, part three, I, B).

<sup>55</sup> Official Records of the General Assembly, Twenty-fourth Session, Supplement No. 18 (A/7618), paras. 63-88 (Yearbook . . . 1968-1970, part two, II, A).



tion in general.<sup>60</sup> It was noted that these contracts were of a complex nature and included elements found also in other types of contracts. It was thought that the contracts would, therefore, form a basis for possible future work in respect of other related contracts.

62. The Commission endorsed the suggestion by the Secretariat that its work in respect of the contracts selected by the Commission should comprise studies of the available literature and the relevant work of other organizations and should analyse international contract practices.<sup>61</sup> The view was also expressed that the Commission should consider the desirability of harmonizing and unifying contractual provisions or clauses commonly occurring in international contracts in the field of industrial development.

63. The report of the Secretary-General submitted to the second session of the Working Group analyses provisions in a number of model contracts, standard contracts and general conditions prepared by other international organizations in respect of contracts for the supply and construction of large industrial works.<sup>62</sup>

#### 5. *Preparation of text for use by other formulating agencies*

##### *Unit of account*

64. The current activity by the Commission in developing a unit of account of constant value for use in conventions which provide for a limitation of liability illustrates another aspect of the role the Commission is called on to fulfil.<sup>63</sup> The various conventions in question have been sponsored by a number of different organizations, both regional and world-wide. Each formulating agency has faced the same problems caused by the change in the role of gold as a measure of constant value. Any one of them could have undertaken the task of redrafting the provisions on the unit of account for use for its own conventions. Indeed, it was the International Civil Aviation Organization which first shifted from the gold franc to the Special Drawing Right as the unit of account in such conventions. However, it is more appropriate that a model clause for use in a large number of conventions be elaborated by an organization whose competence extends across the entire field of international trade law rather than by an organization whose competence is limited to certain aspects of that law. The staff of the International Monetary Fund is actively co-operating with the Commission in this undertaking.

<sup>60</sup> *Official Records of the General Assembly, Thirty-fifth Session, Supplement No. 17 (A/35/17)*, para. 143 (Yearbook . . . 1980, part one, II, A).

<sup>61</sup> *Ibid.*, para. 139.

<sup>62</sup> A/CN.9/WG.V/WP.4 and Add.1-8 (reproduced in this volume, part two, IV, B, 1).

<sup>63</sup> The decision to include such an item in the programme of work of the Commission was made at the eleventh session of the Commission, *Official Records of the General Assembly, Thirty-third Session, Supplement No. 17 (A/33/17)*, para. 67 (Yearbook . . . 1978, part one, II, A).

#### B. *Collection and dissemination of information concerning international trade law*

##### 65. At the first session of the Commission

"29. The view was expressed by the great majority of speakers that the collection and dissemination of information pertaining to international trade law was a matter to which the Commission should give very early consideration. The Commission, it was said, could only have a complete view of what should be accomplished in the field of harmonization and unification, and more usefully expend its efforts to that end, if it had a complete picture of what had already been accomplished. The collection and dissemination of such information would ensure, on the part of the Commission, as well as on the part of other bodies active in the field, that wasteful duplication of effort and of result was avoided. On the basis of such information, the activities of the Commission and of other bodies could be satisfactorily co-ordinated. The circulation of information would make possible the dissemination on an international level of more exact and complete data on activities under way and on the results already achieved in the field of international trade law.

"30. The information to be collected, it was suggested, might include information as to all bodies active in the field of harmonization and unification of international trade law and information as to all work already accomplished and presently undertaken in the field of harmonization and unification. The collection and dissemination of such information was envisaged as a permanent aspect of the work of the Commission. It was thought that it would be appropriate to entrust this function to the Secretariat, which would act as a clearing-house, or documentation centre, for information on international trade law."<sup>64</sup>

66. The Commission has undertaken or contemplated undertaking a number of different activities relevant to the collection and dissemination of information on the harmonization and unification of international trade law.

#### 1. *Publication of information*

##### (a) *Current activities of other organizations*

67. At its first session the Commission decided to compile a register of organizations actively engaged in the progressive harmonization and unification of the law of international trade with a summary of the work which had been accomplished or was being done by them.<sup>65</sup>

<sup>64</sup> *Official Records of the General Assembly, Twenty-third Session, Supplement No. 16 (A/7216)*, paras. 29-30 (Yearbook . . . 1968-1970, part two, I, A).

<sup>65</sup> *Ibid.*, para. 60 subparas. 1-3, 6.



68. This decision was reaffirmed at the second session of the Commission when the subject was discussed under the topic of "Co-ordination of the work of organizations in the field of international trade law" as well as under the topic of "Register of organizations".<sup>66</sup> The Commission was of the opinion that co-operation and exchange of information between organizations on their work would facilitate co-ordination. To that end it requested the Secretary-General to keep other organizations informed about the Commission's work. It also requested the Secretary-General to collect information on the activities of other organizations pertaining to the priority topics included in its programme of work and to make such information available to the Commission on the occasion of its annual sessions.

69. At its third session the Commission again considered the question within the context of establishing a register of organizations, as had been suggested at its second session.<sup>67</sup> The Commission considered two alternative methods by which up-to-date information on the activities of other organizations on matters dealt with by the Commission could be presented: (1) a permanent publication and (2) annual reports by the Secretary-General for the use of members of the Commission. The view was generally held that the second method was an adequate means of providing the Commission with the necessary information and the Commission requested the Secretary-General to submit such a report to the annual sessions of the Commission. This request was reaffirmed by the Commission at its twelfth session<sup>68</sup> and, at the request of the Commission, by the General Assembly, at its thirty-fourth session.<sup>69</sup>

70. Pursuant to this request, since the fourth session of the Commission, the Secretary-General has submitted a report on the work of other organizations in the field of international trade law to each of the annual sessions of the Commission. Commencing with the report submitted to the sixth session of the Commission, these reports on the work of other organizations have been reprinted in the Yearbook, thereby making them permanently available.

#### (b) Register of texts

71. The Commission at its first session decided to publish a register of texts in the English, French, Russian and Spanish languages which would contain:

(a) The text of existing international conventions, model and uniform laws, customs and usages of a multilateral nature which had been published in written form;

(b) A brief summary of proposed international conventions, model and uniform laws, customs and usages of a multilateral nature which were in preparation and had been published in written form.

The registers were, in the first instance to be concerned with:

- (a) The law of sale of goods;
- (b) Standard trade terms;
- (c) Arbitration law;
- (d) Negotiable instruments;
- (e) Documentary credits and the collection of commercial paper.<sup>70</sup>

72. At its second session the Commission confirmed the decision made at its first session to publish a register of texts.<sup>71</sup> There was general agreement that the registers should serve the dual purpose of assisting the Commission in its own work and of providing the outside world (e.g. Governments, universities, organizations, commercial circles) with readily accessible texts of international legal instruments and related material. The list of subjects to be covered in the register was expanded to include the fields of guarantees and securities and of international shipping legislation, those fields having been added to the Commission's programme of work at its second session.

73. At its fourth session the Commission noted that the first volume of the register of texts had been published and authorized the publication of a second volume.<sup>72</sup> This second volume was published in 1973. No further volumes have been published. As a result, the registers of texts do not include the three conventions and two sets of rules for the settlement of disputes which have been produced by the Commission.

#### (c) Yearbook

74. At its second session

"The Commission was of the opinion that it was desirable to establish an UNCITRAL Yearbook to make the Commission's contribution in the field of international trade law more widely known and more readily available beyond the forum of the United Nations."<sup>73</sup>

75. Publication of the first volume of the Yearbook was authorized at the Commission's third session and the

<sup>66</sup> *Ibid.*, Twenty-fourth Session, Supplement No. 18 (A/7618), paras. 134-141, 143-155 (Yearbook . . . 1968-1970, part two, II, A).

<sup>67</sup> *Ibid.*, Twenty-fifth Session, Supplement No. 17 (A/8017), paras. 167-172 (Yearbook . . . 1968-1970, part two, III, A).

<sup>68</sup> *Official Records of the General Assembly, Thirty-fourth Session, Supplement No. 17 (A/34/17)*, para. 131 (Yearbook . . . 1979, part one, II, A).

<sup>69</sup> Resolution 34/142, para. 5 (b) (Yearbook . . . 1980, part one, I, C).

<sup>70</sup> *Official Records of the General Assembly, Twenty-third Session, Supplement No. 16 (A/7216)*, para. 60, subparas. 1, 4-6 (Yearbook . . . 1968-1970, part two, I, A).

<sup>71</sup> *Ibid.*, Twenty-fourth Session, Supplement No. 18 (A/7618), para. 141 (Yearbook . . . 1968-1970, part two, II, A).

<sup>72</sup> *Official Records of the General Assembly, Twenty-sixth Session, Supplement No. 17 (A/8417)*, para. 131 (Yearbook . . . 1971, part one, II, A).

<sup>73</sup> *Ibid.*, Twenty-fourth Session, Supplement No. 18 (A/7618), para. 162 (Yearbook . . . 1968-1970, part two, II, A).

second volume at its fourth session.<sup>74</sup> At its fifth session the Commission decided that the Yearbook should be published on an annual basis as soon as practicable following the Commission's session to which the particular volume related.<sup>75</sup> "Such annual publication of the *Yearbook* would enable legal and business circles to follow the work of the Commission more closely and provide the means for the timely examination and evaluation of the Commission's work."<sup>76</sup>

#### (d) Bibliography

76. The Commission at its first session requested the Secretary-General to inquire whether one or more universities, research or similar institutions in the States members of the United Nations would be willing to compile and disseminate a list of published books, articles and commentaries on those international conventions, model and uniform laws, customs and usages of a multilateral nature which were to be included in the register of texts.<sup>77</sup>

77. In accordance with the request of the Commission, the Parker School of Foreign and Comparative Law began the preparation of a bibliography on international trade law. A sample of the bibliography dealing with the materials on arbitration was presented to the Commission at its second session.<sup>78</sup>

78. At the third session of the Commission further bibliographies on international sale of goods, standard trade terms, negotiable instruments and bankers' commercial credits were presented to the Commission.<sup>79</sup> In a report to the Commission at that session the Secretary-General pointed out that the bibliography was being compiled without compensation by the Parker School of Foreign and Comparative Law of Columbia University but that it did not appear feasible to expect an institution to contribute such services indefinitely.<sup>80</sup>

79. The Commission was of the opinion that various alternative ways of expanding the bibliographies without expenditure should be explored before requesting the General Assembly to make funds available to support further work on bibliographies.<sup>81</sup>

80. The Secretary-General reported to the Commission at its fourth session that it did not appear feasible to have bibliographies prepared on the priority topics of the Commission's programme of work on a voluntary basis and that the cost of having it done by staff of the Secretariat would be prohibitively expensive.<sup>82</sup> However, as an alternative a "Survey of Bibliographies Relating to International Trade Law" was presented to the Commission with the suggestion that it might be considered to sufficiently meet current needs.<sup>83</sup>

81. At its fourth session, the Commission requested the Secretary-General to invite members of the Commission to provide him with bibliographies relating to subject-matters included in the work of the Commission.<sup>84</sup> Bibliographical materials were subsequently supplied by Australia, Austria, Belgium, Brazil, Chile, Hungary, Italy, Romania, the United Kingdom of Great Britain and Northern Ireland and the Union of Soviet Socialist Republics.<sup>85</sup>

82. At its third session the Commission, consistent with its desire that alternative ways be found to have bibliographies prepared without requesting funds from the General Assembly, authorized the inclusion of a bibliography on the Commission and its work in the first volume of the Yearbook.<sup>86</sup> Each subsequent volume of the Yearbook has contained a bibliography of materials on the Commission and its work prepared by the Secretariat. In preparing the bibliography the Secretariat has been deeply grateful for the suggestions made to it by members of the Commission and other interested persons of items to be included.

#### (e) Teaching materials

83. The report of the Secretary-General to the third session of the Commission on training and assistance in the field of international trade law suggested "that an effective tool for the dissemination of international trade law, particularly in developing countries, may be through preparation of teaching materials. Such materials might serve various functions: to introduce law students in various countries to this developing body of law and also to help make this material more readily available to teachers, government officials and practitioners."<sup>87</sup>

84. The Commission agreed with this suggestion and requested the Secretary-General "to consult with

<sup>74</sup> *Ibid.*, Twenty-fifth Session, Supplement No. 17 (A/8017), para. 209 (Yearbook . . . 1968-1970, part two, III, A); *ibid.*, Twenty-sixth Session, Supplement No. 17 (A/8417), para. 135 (Yearbook . . . 1971, part one, II, A).

<sup>75</sup> *Ibid.*, Twenty-seventh Session, Supplement No. 17 (A/8717), para. 104 (Yearbook . . . 1972, part one, II, A).

<sup>76</sup> *Ibid.*, para. 102. The Secretariat regrets that the publication of Volume IX of the Yearbook has been delayed due to the transfer of the Commission's Secretariat from New York to Vienna. It is hoped that the prompt publication of the Yearbook will soon be restored.

<sup>77</sup> *Ibid.*, Twenty-third Session, Supplement No. 16 (A/7216), para. 60, subpara. 7 (Yearbook . . . 1968-1970, part two, I, A).

<sup>78</sup> A/CN.9/24/Add.1.

<sup>79</sup> A/CN.9/R.3.

<sup>80</sup> A/CN.9/43.

<sup>81</sup> *Official Records of the General Assembly, Twenty-fifth Session, Supplement No. 17 (A/8017)*, paras. 179-186 (Yearbook . . . 1968-1970, part two, III, A).

<sup>82</sup> A/CN.9/L.20.

<sup>83</sup> A/CN.9/L.20/Add.1 (Yearbook . . . 1971, part two, Bibliographies, 1).

<sup>84</sup> *Official Records of the General Assembly, Twenty-sixth Session, Supplement No. 17 (A/8417)*, para. 137 (Yearbook . . . 1971, part one, II, A).

<sup>85</sup> These materials were published in document A/CN.9/L.25 (Yearbook . . . 1974, part three, II, A).

<sup>86</sup> The proposal that a bibliography be included was made in A/CN.9/32/Add.1, Annex I.

<sup>87</sup> A/CN.9/39, para. 11.

appropriate institutions on the feasibility of developing teaching materials in the subject matter of this field".<sup>88</sup>

85. The Commission was informed at its fourth session that one organization had shown interest in the project and was developing plans for the production of these materials for use in Africa and Latin America.<sup>89</sup> However, at its fifth session the Commission was informed that there had been changes in the programmes of that organization and it was no longer planning on producing the envisaged teaching materials.<sup>90</sup>

86. At the fifth session of the Commission "some representatives emphasized the importance of the project relating to the development of teaching materials on the subject of international trade law, and hoped that the Secretariat would succeed in its . . . efforts to secure funds for this project."<sup>91</sup> Subsequently, at the sixth and seventh sessions Australia offered a sum of money to enable a young scholar from a developing country to undertake the compilation of such materials in Australia.<sup>92</sup>

## 2. Other means of disseminating information

### (a) Training and assistance

87. Within the Commission, it has always been understood that the Commission's activities in training and assistance would have the dual function of "increasing" the opportunities for the training of experts in the field of international trade law, particularly in many of the developing countries" and of "exposing interested persons in the particular countries and regions (where the Commission might hold seminars) to a more intense awareness of the work of the Commission."<sup>93</sup>

88. In order to better define the concept of international trade law, the Commission, at its sixth session, decided to organize, in connexion with its eighth session, an international symposium on the role of universities and research centres in the teaching, dissemination and wider appreciation of international trade law.<sup>94</sup> It had been suggested in the report of the Secretary-General that "A general discussion on the proposed theme for the symposium would throw light on the nature and scope of

international trade law and assess, in a more deliberate manner, the feasibility of introducing the subject in the curricula of national universities."<sup>95</sup>

89. Similarly, when the Commission decided at its thirteenth session to hold a second symposium on the occasion of its fourteenth session, "There was general agreement that the subject-matter to be discussed at the symposium should cover those matters in which UNCITRAL is or had been active, in particular, arbitration and conciliation, sales, maritime law and the legal implications of the new international economic order."<sup>96</sup>

### (b) Active participation of international organizations

90. As has already been discussed above, throughout the discussions in the Sixth Committee which led to the adoption of resolution 2205 (XXI), by which the Commission was created, there had been frequent mention of the contributions of existing formulating agencies to the harmonization and unification of international trade law and of the need for the new commission to co-operate with those agencies in the future. Therefore, the General Assembly in paragraphs 11 and 12 of resolution 2205 (XXI) provided that:

"11. The Commission may consult with or request the services of any international or national organization, scientific institution and individual expert, on any subject entrusted to it, if it considers such consultation or services might assist it in the performance of its functions.

"12. The Commission may establish appropriate working relationships with intergovernmental organizations and international non-governmental organizations concerned with the progressive harmonization and unification of the law of international trade."

91. In accordance with the indications given by the General Assembly, when the Secretary-General undertook the organization of the Commission's first session, he invited a number of international organizations to attend. Those organizations fell into two groups.<sup>97</sup> The first group consisted of the Hague Conference on Private International Law, the International Institute for the Unification of Private Law (UNIDROIT) and the United International Bureau for the Protection of Intellectual Property, with which the United Nations had existing agreements providing for reciprocal representation at meetings, and UNCTAD, which is specifically mentioned in resolution 2205 (XXI). The second group consisted of specialized agencies of the United Nations system, other intergovernmental organizations and international non-governmental organizations which, in replying to the

<sup>88</sup> *Official Records of the General Assembly, Twenty-fifth Session, Supplement No. 17 (A/8017)*, para. 200 (Yearbook . . . 1968-1970, part two, III, A).

<sup>89</sup> A/CN.9/58, para. 13.

<sup>90</sup> A/CN.9/65, para. 6.

<sup>91</sup> *Official Records of the General Assembly, Twenty-seventh Session, Supplement No. 17 (A/8717)*, para. 91 (Yearbook . . . 1972, part one, II, A).

<sup>92</sup> *Official Records of the General Assembly, Twenty-eighth Session, Supplement No. 17 (A/9017)*, para. 93 (Yearbook . . . 1973, part one, II, A); *ibid.*, *Twenty-ninth Session, Supplement No. 17 (A/9617)*, para. 72 (Yearbook . . . 1974, part one, II, A).

<sup>93</sup> *Ibid.*, *Twenty-third Session, Supplement No. 16 (A/7216)*, para. 67 and *ibid.*, *Twenty-fifth Session, Supplement No. 17 (A/8017)*, para. 195 (Yearbook . . . 1968-1970, part two, I, A and part two, III, A).

<sup>94</sup> *Ibid.*, *Twenty-eighth Session, Supplement No. 17 (A/9017)*, para. 107 (Yearbook . . . 1973, part one, II, A).

<sup>95</sup> A/CN.9/80, para. 16.

<sup>96</sup> *Official Records of the General Assembly, Thirty-fifth Session, Supplement No. 17 (A/35/17)*, para. 158 (Yearbook . . . 1980, part one, II, A).

<sup>97</sup> A/CN.9/7, paras. 10-14.

invitation of the Secretary-General pursuant to resolution 2205 (XXI), had sent comments on a programme of work to be undertaken by the Commission or had manifested their interest by describing their own activities or expressing readiness to collaborate with the Commission.

92. At its second session, when it first considered the question, the Commission was of the opinion that the informal methods of collaboration with other organizations used up to that time had produced satisfactory results and should be continued. Specifically, it requested the Secretary-General to make arrangements for the attendance of observers of international organizations similar to those made for the second session.<sup>98</sup>

93. Consequently, throughout the history of the Commission, intergovernmental organizations and international non-governmental organizations interested in international trade law have been invited to send observers to attend sessions of the Commission and of inter-sessional working groups, and have been consulted on specific subjects in which they were interested.

(c) *Global participation in activities of the Commission*

94. Although interested international organizations had been invited to send observers to the annual sessions of the Commission, States which were not members of the Commission were neither invited to send observers nor allowed to do so. This was in implementation of the decision of the General Assembly to allocate the membership of the Commission among the five geographical regions of the world.

95. At the seventh session of the Commission, the question arose whether the draft text of the revised rules on the responsibility of ocean carriers as it would be adopted by the Working Group on International Legislation on Shipping would be sent to all Governments for comment prior to consideration by the Commission or only to States members of the Commission. After discussion the Commission agreed that the draft text should be given the widest possible distribution to Governments and interested international organizations prior to the discussion of the draft text by the Commission.<sup>99</sup> The question was again discussed at the eighth session of the Commission in respect of the draft text of the revised Uniform Law on the International Sale of Goods to be adopted by the Working Group on the International Sale of Goods.<sup>100</sup> The precedent established in respect of the draft text of the revised rules on the responsibility of

ocean carriers was followed. Since that time it has been accepted practice by the Commission that whenever comments or proposals of Governments are solicited, all Governments will be invited to respond and not just those States members of the Commission.

96. The Sixth Committee has noted with approval the Commission's procedure of circulating draft legal texts prepared by its working groups to Governments and to interested international organizations for comment before adopting a final (draft) text. It was the view of the Sixth Committee "that that practice enabled the Commission to benefit from the broadest range of views in its preparation of texts."<sup>101</sup>

97. The Commission turned to the question of States not members of the Commission participating in the work of the Commission as observers at its ninth session.<sup>102</sup> It noted that at various sessions of the Commission and of its Working Groups several Governments that were not members of the Commission had expressed the wish to attend as observers. The Commission was of the opinion that it would be in the interest of the Commission's work to have broad participation at the preliminary stages of preparation of a text so as to enhance its acceptability at a later time. Therefore, it recommended to the General Assembly that States not members of the Commission be permitted to attend sessions of the Commission and its Working Groups as observers. The General Assembly agreed with this recommendation in resolution 31/99 of 15 December 1976,\* para. 10 (c).

98. Although the Commission has not established formal rules in respect of observers, it has generally accorded them the same right to speak and to submit proposals as is accorded a member of the Commission. It has been thought that a text of international trade law should reflect the interests of all participants in international trade. Therefore, in order to reach an effective consensus, it was desirable that all relevant points of view be expressed and considered at as early a stage as possible in the preparation of the text.

### PART III. QUESTIONS OF METHODOLOGY

99. The adoption of a new programme of work by the Commission at its eleventh session as a result of the completion, or contemplated completion, of the items on the Commission's original programme of work has brought with it a certain diversity in the methodology of

<sup>98</sup> Official Records of the General Assembly, Twenty-fourth Session, Supplement No. 18 (A/7618), para. 155 (Yearbook . . . 1968-1970, part two, II, A).

<sup>99</sup> Official Records of the General Assembly, Twenty-ninth Session, Supplement No. 17 (A/9617), para. 53 (Yearbook . . . 1974, part one, II, A).

<sup>100</sup> Ibid., Thirtieth Session, Supplement No. 17 (A/10017), paras. 15, 17 (Yearbook . . . 1975, part one, II, A).

\* Yearbook . . . 1977, part one, I, C.

<sup>101</sup> Ibid., Thirty-first Session, Annexes, agenda item 108 (A/31/390), para. 10 (Yearbook . . . 1977, part one, I, B).

<sup>102</sup> Ibid., Supplement No. 17 (A/31/17), para. 74 (Yearbook . . . 1976, part one, II, A).

the Commission in its approach to the legal issues of international trade. This part of the report discusses some aspects of that diversity in methodology.

### A. *Final form of texts*

#### 1. *In general*

100. During the Commission's first 10 years of existence it undertook work in four fields of interest: the law of international sales of goods, carriage of goods by sea, international negotiable instruments and international commercial arbitration. In spite of the evident differences between these four subjects, they have several common characteristics which made them particularly suitable for the Commission's initial efforts. All four of the subjects are fundamental to the law governing international trade transactions and the resolution of commercial disputes arising out of such transactions. There is an abundant literature on the law within the various legal systems, on the differences between the legal systems, and on the practical importance of those differences. Successful work in each of these four areas has been seen to contribute to the reduction of barriers to trade and undertaking the work has been obviously of value.

101. Each of the four areas lent itself to comprehensive texts. In respect of international sales of goods, carriage of goods by sea and international negotiable instruments, international conventions intended to become the basic law in a major field were appropriate. It was not thought necessary to prepare a new convention on international commercial arbitration, but the UNCITRAL Arbitration Rules were designed so as to be applicable to any form of international commercial dispute and were expected to serve as a model upon which institutional arbitration rules might be based, a process which has already begun.

102. The subjects on which the Commission decided to suspend any further action, the preparation of general conditions of sale for use in a wide range of commodity trades, products liability and security interests were also subjects in which a comprehensive text was envisaged.<sup>103</sup>

103. The subject matter of the Commission's new programme of work does not always require a comprehensive solution, as did the original programme of work. For example, at this session the Commission will decide whether to adopt guidelines for administering arbitra-

tions under the UNCITRAL Arbitration Rules.<sup>104</sup> These guidelines would be addressed to arbitral institutions which have indicated their willingness to act as appointing authorities or to provide administrative services for arbitrations conducted under the Rules. If adopted, the guidelines would ensure that the UNCITRAL Arbitration Rules were, to the extent possible, left unchanged by the administering institution.

104. The guidelines would serve an important function, but not one of the same magnitude as do the Rules themselves. Similarly, the proposed uniform rules on liquidated damages and penalty clauses would provide rules to govern a problem which is difficult and important, but the proposed rules are not of the same magnitude in scope as, for example, the Commission's work in respect of the international sale of goods.

105. The difference in magnitude of the problems considered may have an impact on the final form which the Commission's work might take. This is true of both the draft guidelines and the draft uniform rules on liquidated damages and penalty clauses.<sup>105</sup> In both cases a certain economy of effort may be appropriate.

106. The guidelines would be, for the first time in the Commission's experience, cast in the form of recommendations rather than in the form of proposed rules ready for adoption. The individual administering arbitration institutions would be invited to review their administrative rules as to their compatibility with the UNCITRAL Arbitration Rules and to draw up, if necessary, new rules which would take account of local conditions and their own administrative structure.

107. The guidelines approach may be feasible when it would not be feasible to propose a text ready for adoption. Moreover, in some cases, the development of guidelines or recommendations may be an appropriate first objective, leaving until later a decision as to whether further actions are desirable. This would seem to be the case in respect of contracts for the supply and construction of large industrial works.

108. The Commission at its thirteenth session decided that in respect of its work on legal aspects of the new international economic order it would accord priority to work related to contracts in the field of industrial development and requested the Secretary-General to carry out preparatory work on contracts for the supply and construction of large industrial works and on industrial co-operation.<sup>106</sup> It was noted that these contracts

<sup>103</sup> For the Commission's actions in respect of products liability and security interests, see Report of the United Nations Commission on the work of its tenth session, *Official Records of the General Assembly, Thirty-second Session, Supplement No. 17 (A/32/17)*, para. 44 (Yearbook . . . 1977, part one, II, A), and Report of the United Nations Commission on International Trade Law on the work of its thirteenth session, *ibid.*, *Thirty-fifth Session, Supplement No. 17 (A/35/17)*, para. 28 (Yearbook . . . 1980, part one, II, A).

<sup>104</sup> The draft guidelines are contained in a note by the Secretary-General submitted to the thirteenth session, A/CN.9/189 (Yearbook . . . 1980, part two, IV, D). The Commission at its thirteenth session decided to postpone until its fourteenth session the consideration of the draft guidelines.

<sup>105</sup> See paras. 114 to 122, below.

<sup>106</sup> *Official Records of the General Assembly, Thirty-fifth Session, Supplement No. 17 (A/35/17)*, para. 143 (Yearbook . . . 1980, part one, II, A).

were of a complex nature and included elements found also in other types of contracts. It was thought that these contracts would, therefore, form a basis for possible future work in respect of other related contracts.<sup>107</sup>

109. The Secretary-General has submitted to the second session of the Working Group on the New International Economic Order, which meets from 9 to 18 June 1981 at Vienna, the first half of the study in respect of contracts for the supply and construction of large industrial works.<sup>108</sup> The study analyses clauses found in a number of general conditions, model contracts or draft model contracts. The study suggests that a preliminary objective of the Commission's work might be the preparation of a legal guide in order to assist parties in the negotiation of contracts.<sup>109</sup>

110. The study points out that there are already in existence several guides or guidelines such as those prepared by the Economic Commission for Europe (ECE) and the United Nations Industrial Development Organization (UNIDO) but that the ECE Guide is addressed to enterprises in Europe and is rather brief while the various UNIDO documents deal mainly with economic, technical, administrative and financial aspects of the installation of large industrial works.

111. The study also suggests that as work progresses on such a guide, a stage may be reached when a model clause approach would be feasible in the context of some clauses, or perhaps a uniform law approach would be appropriate in the light of conflicting national rules as regards other legal issues.

112. A comprehensive legal guide which would identify the legal issues to be kept in mind when negotiating and drafting contracts on large industrial works, describe various approaches pointing out the advantages and disadvantages of each approach and suggest alternative solutions would itself be an important contribution, especially to the developing countries. Contracts for the supply and construction of large industrial works are complex and the provisions are inter-related. The negotiation and drafting of an agreement which fairly represents the interests of all parties is less likely if they possess a significant difference in technical expertise. A comprehensive guide would, therefore, be of particular value to the developing countries which, as a rule, have less expertise in such matters.

113. The experience gained in preparing the guide would also benefit the Commission itself in any later work it might undertake in respect of contracts for the supply and construction of large industrial works or of similar types of contract.

## 2. *Draft rules on liquidated damages and penalty clauses: an example*

114. When the Working Group on International Contract Practices approved the text of the draft rules at its second session in New York from 13 to 17 April 1981, it decided that the question as to the form which these rules should take should be left for decision by the Commission.<sup>110</sup> The Working Group did not make any recommendation but one representative stated that the business community in his country was of the view that it would not be useful to cast the uniform rules in the form of law.

115. The draft rules relate to the response of the legal system to a liquidated damages or penalty clause in a contract. This is a legal problem which cannot be solved by the contract itself. Therefore, if the rules are to be effective, they must be adopted by the legal system and cannot be in the form of draft contract clauses.

116. The Commission might adopt the rules in the form of a convention, in the form of a model law or in the form of recommendations. The advantages and disadvantages of each form are discussed below.

### (a) *Convention*

117. The normal form for a text on the unification of international trade law is a convention, and it is the form which the Commission has used on three prior occasions. It is a well known method and presents no serious procedural difficulties. In all legal systems once the State has become a party to a convention, the convention, or a text containing the language of the convention, becomes the law governing the transactions that fall within its scope of application.

118. A convention can be adopted by a conference of plenipotentiaries or by the General Assembly on the recommendation of the Sixth Committee. The Commission will have before it at this session a note by the Secretariat on alternative procedures available for the adoption of the Commission's draft conventions which will discuss the advantages and disadvantages of these two methods.<sup>111</sup>

119. There would be two major disadvantages to adopting the draft rules by means of a convention rather than as a model law or as recommendations. The first is that the further consideration of the text by a conference of plenipotentiaries or the Sixth Committee, would add expense both to the United Nations and to the States. The second is that the constitutional and political procedures for a State to become a party to a convention on international trade law be more complicated than are the procedures for ordinary domestic legislation.

<sup>107</sup> *Ibid.*, para. 136.

<sup>108</sup> A/CN.9/WG.V/WP.4 and Add.1 to 8 (reproduced in this volume, part two, IV, B, 1).

<sup>109</sup> A/CN.9/WG.V/WP.4, para. 41 (reproduced in this volume, part two, IV, B, 1).

<sup>110</sup> Report of the Working Group on International Contract Practices on the work of its second session, A/CN.9/197 (reproduced in this volume, part two, I, A).

<sup>111</sup> A/CN.9/204 (reproduced in this volume, part two, VIII).



(b) *Model law*

120. The procedure for the adoption of a model law would be the same as the procedure for the adoption of the UNCITRAL Arbitration Rules and the UNCITRAL Conciliation Rules, i.e. the model law would be adopted by the Commission without reference to a conference of plenipotentiaries or to the General Assembly. However, the Commission might wish to request the General Assembly to commend the enactment of the model law, as it requested the General Assembly to commend the use of the two sets of Rules.

121. The adoption of a model law by the Commission is an easier and less costly procedure than the adoption of the same substantive text by a conference of plenipotentiaries. However, detailed consideration of the subject by the Commission alone may not generate the same interest which consideration by a conference of plenipotentiaries would generate and the likelihood of subsequent adoption by States may be reduced thereby.

(c) *Recommendation*

122. The procedure for the adoption of the draft rules in the form of a recommendation would be the same as for the adoption of a model law. The major difference would be that if the Commission were to adopt the draft rules as a model law, it would at the same time recommend that States adopt the model law by legislative action. If the Commission were to adopt the draft rules in the form of a recommendation, it would simply urge that States apply the substance of the rules to international contracts. The exact form in which the State would follow the recommendation would be immaterial. For example, if a State already applied the substance of the draft rules to international contracts by virtue of its existing domestic legislation or judicial practice, no further action by the State would be necessary.

B. *Endorsements of texts prepared by other agencies*

123. Whenever the Commission has endorsed a text prepared by another formulating agency, it has been the Commission itself which has taken the initiative. For example, the Commission at its first session requested the Secretary-General to invite the International Chamber of Commerce to submit a report including its views and suggestions concerning possible action that might be taken for the purpose of promoting the wider use of Incoterms and other trade terms by those engaged in international commerce.<sup>112</sup>

124. This request by the Commission elicited a report from the International Chamber of Commerce in respect of Incoterms that led to their endorsement by the Commission at its second session. The request by the Commission was the commencement of a long and fruitful collaboration between the Commission and the International Chamber of Commerce.

125. In recent years, however, the Commission has not sought out for endorsement texts adopted by other formulating agencies. This does not appear to have been a conscious policy so much as a reflection of the full programme of work which has characterized the recent sessions of the Commission. Now that the mandate of the Commission in the co-ordination of legal activities in the field of international trade law has been reaffirmed by the General Assembly, the Commission may wish to consider actively soliciting additional texts for endorsement.

126. The report on current activities of international organizations related to the harmonization and unification of international trade law contains every year a report on draft conventions, model laws, general conditions, trade terms, guides and guidelines which are in the course of preparation or which have been adopted by various intergovernmental and international non-governmental organizations. Some of these texts may be appropriate for endorsement by the Commission.<sup>113</sup>

C. *Publications of texts adopted and endorsed by the Commission*

127. It has been noted above that volume II of the Register of Texts of Conventions and other Instruments concerning International Trade Law was published in 1973 and that, as a result, the Register of Texts does not include any of the texts adopted by the Commission.<sup>114</sup> For the same reason the Register of Texts does not include other important texts concerning international trade law adopted in the past eight years, such as the 1974 revision of Uniform Customs and Practice for Documentary Credits<sup>115</sup> or the 1980 revision of Incoterms.

128. A new publication, perhaps in the form of a third volume of the Register of Texts containing the texts adopted by the Commission would be desirable.<sup>116</sup> However, the function of this publication might be somewhat

<sup>112</sup> This year's report is in A/CN.9/202 and Add.1 and 2 (reproduced in this volume, part two, V, A).

<sup>114</sup> See para. 73 above.

<sup>115</sup> See para. 15 above.

<sup>116</sup> The funds for a third volume of the Register of Texts were already provided in the regular budget of the Commission for the biennium 1980-1981. The Secretariat has requested that funds should similarly be included for the biennium 1982-1983.

<sup>112</sup> *Official Records of the General Assembly, Twenty-third Session, Supplement No. 16 (A/7216), para 48 (20) (Yearbook . . . 1968-1970, part two, I, A).*



different from that of the two volumes of the Register of Texts already published. While the Register of Texts was intended to "serve the dual purpose of assisting the Commission in its own work and of providing the outside world (e.g. Governments, universities, organizations, commercial circles) with readily accessible texts of international legal instruments and related material"<sup>117</sup> the new publication might serve as a repository of the newly developing *lex mercatoria* as it emerges from the work of the Commission. In such a case the publication would also contain those texts endorsed by the Commission. In addition, the publication might contain introductory chapters which describe the activities of the Commission for the harmonization and unification of international trade law. It could be envisaged that in time the texts adopted and endorsed by the Commission would contain the content, if not the form, of an international trade code.

129. It could be expected that such a publication would aid in the promotion of the texts which were included. This may be seen to be of particular importance in the case of the three conventions adopted to date on the basis of a draft convention prepared by the Commission, none of which are as yet in force. In addition, inclusion in the publication of the texts endorsed by the Commission would increase the significance of the endorsement.

130. Moreover, a publication which contained the texts prepared and endorsed by the Commission would serve as an excellent source of documentary materials on international trade law. This would benefit teachers, practitioners and students alike. Even where libraries are adequate, the process of finding the relevant texts can be time consuming. Where the libraries are not adequate, which is unfortunately often the case, it may not be possible to find the texts at all. Therefore, the publication would also further the Commission's programme of training and assistance in international trade law.

#### CONCLUSIONS

131. During the first 14 years of the Commission's existence it has developed working methods that have permitted it to make an important contribution to the harmonization and unification of international trade law. It has produced three conventions and two sets of procedural rules for optional use by parties to a dispute

arising out of international trade. It has endorsed texts adopted by other organizations and has referred yet other texts to regional economic organizations for their consideration. It has engaged in a programme of information which has increased knowledge about international trade law. It has attempted to the extent possible to co-ordinate the multitude of formulating agencies engaged in the harmonization and unification of international trade law at both regional and universal level.

132. In order to strengthen its role as the central agency for the unification and harmonization of international trade law, the Commission may wish to consider the following recommendations.

133. The Commission may wish to reaffirm that its purpose is the harmonization and unification of the law of international trade. It recognizes that many formulas are appropriate for the rules which make up the law of international trade. It notes that resolution 2205 (XXI) mentions by way of example conventions, model and uniform laws, trade terms, provisions, customs and practice, but that other formulas, such as recommendations, guidelines and checklists, have been used by various formulating agencies and that yet other formulas may be appropriate in certain circumstances.

134. The Commission may wish to note that in its first several sessions it actively looked for existing texts prepared by other formulating agencies so that it might endorse those texts and encourage their increased use. It may further wish to note that its actions in so doing has had the additional effect of increasing co-operative activities with those other agencies. The Commission may wish to reaffirm its belief that this is an effective means to promote the harmonization and unification of international trade law.

135. The Commission may wish to reaffirm that the texts adopted and endorsed by it constitute an important contribution to the harmonization and unification of international trade law. The Commission may wish, therefore, to request the Secretary-General to publish those texts, with explanatory chapters to introduce the activities of the Commission, in an appropriate form under the regular budget appropriated for the publication of the Register of Texts, not only so that they would individually be more easily available, but also so that the contribution of the Commission to the work in this field would be more meaningful.

136. The Commission may also wish to request the Secretary-General further to strengthen contact with the other formulating agencies active in the field of international trade law with a view to ascertaining if any further co-operative arrangements could be made to promote the goals of the Commission, including the avoidance of duplication of work.

<sup>117</sup> Report of the United Nations Commission on International Trade Law on the work of its second session, *Official Records of the General Assembly, Twenty-fourth Session, Supplement No. 18* (A/7618), para. 136 (Yearbook . . . 1968-1970, part two, II, A).

## C. Note by the Secretariat: co-ordination of activities (A/CN.9/208)\*

The resolution contained in the annex to this note was adopted by the Asian-African Legal Consultative Committee on 30 May 1981 at its twenty-second session held in Colombo, Sri Lanka.

## ANNEX

*The Asian-African Legal Consultative Committee (AALCC)*

*Noting* with satisfaction the existing close collaboration of work between the AALCC and the United Nations Commission on International Trade Law (UNCITRAL);

*Expressing* its view that the aims which the new international economic order sought to achieve would, in respect of UNCITRAL, be best served if an approach similar to that taken as regards the United Nations Convention on the Carriage of Goods by Sea (Hamburg Rules, 1978)\*\* would permeate the other work of UNCITRAL;

*Noting* with appreciation that UNCITRAL has successfully led to the adoption of the United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980);\*\*\*

*Further noting* with appreciation:

(a) The adoption of the UNCITRAL Conciliation Rules (1980),\* which would help in the expeditious and amicable settlement of disputes in international transactions, particularly in the Asian-African region;

(b) The decision of UNCITRAL, in response to the views expressed by the AALCC at its 17th, 18th and 20th sessions, to commence work to prepare a model arbitration law which if widely adopted by States in their domestic legislation would further eliminate barriers to the promotion of international commercial arbitration; and

(c) The decision of UNCITRAL, upon the endorsement of the AALCC at its 21st session, to commence studies on contracts for the supply and construction of large industrial works in the context of the new international economic order;

*Expresses* its continued support to the work programme of UNCITRAL;

*Recommends* to the governments of the member States to consider the possibility of ratifying or adhering to the United Nations Convention on Carriage of Goods by Sea (Hamburg Rules, 1978) and the United Nations Convention on Contracts for the International Sale of Goods (1980); and

*Requests* its Secretary-General to draw the attention of Governments of member States to the importance of having their representatives or observers participate in the sessions of UNCITRAL and its subordinate organs.

\* Yearbook . . . 1980, part three, II.

\* 5 June 1981. Referred to in Report, paras. 88, 97, 115 (part one, A, above).

\*\* Yearbook . . . 1978, part three, I, B.

\*\*\* Yearbook . . . 1980, part three, I, B.

## VI. STATUS OF CONVENTIONS\*

Note by the Secretary-General: status of conventions (A/CN.9/205/Rev.1)\*\*

1. At its thirteenth session the Commission decided that it would consider, at each of its sessions, the status of conventions that were the outcome of work carried out by it.<sup>1</sup>

2. The present note is submitted pursuant to that decision. The annex hereto sets forth the state of signatures, ratifications and accessions as at 26 June 1981 to the following conventions: Convention on the Limitation Period in the International Sale of Goods (New York, 1974); Protocol amending the Convention on the Limitation Period in the International Sale of Goods (Vienna, 1980); United Nations Convention on the Carriage of Goods by Sea, 1978 (Hamburg); and United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980).

### ANNEX

1. Convention on the Limitation Period in the International Sale of Goods (New York, 1974):\*\*\*

State	Signature	Ratification	Accession
Brazil	14 June 1974		
Bulgaria	24 February 1975		
Byelorussian SSR	14 June 1974		
Costa Rica	30 August 1974		
Czechoslovakia	29 August 1975	26 May 1977	
Dominican Republic			23 December 1977
German Democratic Republic	14 June 1974		
Ghana	5 December 1974	7 October 1975	
Hungary	14 June 1974		
Mongolia	14 June 1974		
Nicaragua	13 May 1975		

State	Signature	Ratification	Accession
Norway	11 December 1975	20 March 1980	
Poland	14 June 1974		
Ukrainian SSR	14 June 1974		
USSR	14 June 1974		
Yugoslavia			27 November 1978

Signatures only: 11; ratifications: 3; accessions: 2.

2. Protocol amending the Convention on the Limitation Period in the International Sale of Goods (Vienna, 1980):\*

No accessions up to date.

3. United Nations Convention on the Carriage of Goods by Sea, 1978 (Hamburg):\*\*

State	Signature	Ratification	Accession
Austria	30 April 1979		
Barbados			2 February 1981
Brazil	31 March 1978		
Chile	31 March 1978		
Czechoslovakia	6 March 1979		
Denmark	18 April 1979		
Ecuador	31 March 1978		
Egypt	31 March 1978	23 April 1979	
Finland	18 April 1979		
France	18 April 1979		
Germany, Federal Republic of	31 March 1978		
Ghana	31 March 1978		
Holy See	31 March 1978		
Hungary	23 April 1979		
Madagascar	31 March 1978		
Mexico	31 March 1978		
Morocco			12 June 1981
Norway	18 April 1979		
Pakistan	8 March 1979		
Panama	31 March 1978		
Philippines	14 June 1978		
Portugal	31 March 1978		
Senegal	31 March 1978		
Sierra Leone	15 August 1978		
Singapore	31 March 1978		
Sweden	18 April 1979		
Tunisia			15 September 1980
Uganda			6 July 1979
United Republic of Tanzania			24 July 1979

\* For consideration by the Commission see Report, chapter VIII (part one, A, above).

\*\* 10 July 1981. Referred to in Report, para. 112 (part one, A, above).

\*\*\* A/CONF.63/15 (Yearbook . . . 1974, part three, I, B).

<sup>1</sup> Report of the United Nations Commission on International Trade Law on the work of its thirteenth session, *Official Records of the General Assembly, Thirty-fifth Session, Supplement No. 17 (A/35/17)*, para. 163 (Yearbook . . . 1980, part one, II, A).

\* A/CONF.97/18, annex II (Yearbook . . . 1980, part three, I, C).

\*\* A/CONF.89/13, annex I (Yearbook . . . 1978, part three, I, B).

<i>State</i>	<i>Signature</i>	<i>Ratification</i>	<i>Accession</i>
United States of America	30 April 1979		
Venezuela	31 March 1978		
Zaire	19 April 1979		

Signatures only: 26; ratification: 1; accessions: 5.

4. United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980):\*

<i>State</i>	<i>Signature</i>	<i>Ratification</i>	<i>Accession</i>
Austria	11 April 1980		
Chile	11 April 1980		

<i>State</i>	<i>Signature</i>	<i>Ratification</i>	<i>Accession</i>
Denmark	26 May 1981		
Finland	26 May 1981		
Germany, Federal Republic of	26 May 1981		
Ghana	11 April 1980		
Hungary	11 April 1980		
Lesotho	18 June 1981	18 June 1981	
Netherlands	29 May 1981		
Norway	26 May 1981		
Singapore	11 April 1980		
Sweden	26 May 1981		
Yugoslavia	11 April 1980		

Signatures only: 12; ratification: 1.

\* A/CONF.97/18, annex I (Yearbook . . . 1980, part three, I, B).

## VII. TRAINING AND ASSISTANCE IN THE FIELD OF INTERNATIONAL TRADE LAW\*

### Report of the Secretary-General: training and assistance: possibility of holding regional seminars (A/CN.9/206)\*\*

1. The Commission at its thirteenth session requested the Secretary-General to "report to it on the possibility of holding regional seminars."<sup>1</sup> The present report is submitted in response to that request. In order to evaluate the desirability of holding regional seminars, certain aspects of the administration of the First and Second UNCITRAL Symposia on International Trade Law are also discussed.

2. Both the Commission and the General Assembly have consistently emphasized the value of a programme of training and assistance in international trade law through the holding of seminars and symposia.<sup>2</sup> Such a programme has the dual function of training young lawyers, particularly from developing countries, in international trade law and of promoting the unification and harmonization of international trade law by making the relevant texts more widely known.

3. The two symposia which the Commission has sponsored to date have been held on the occasion of an annual session of the Commission.<sup>3</sup> At the thirteenth session it was suggested that doing so had the advantage that the Commission was more immediately involved than if a symposium were held at any other time or place.<sup>4</sup> In addition, participants in the symposium can become better acquainted with the work of the Commission itself.

4. On the other hand it was suggested that the holding of regional seminars might have greater impact both because more participants from the region might be able to attend and because of the local publicity which would be generated.<sup>5</sup>

5. In the light of these considerations, it would seem to be desirable to organize, if possible, a series of seminars and symposia on various aspects of international trade law, both on the occasion of the Commission's annual sessions and on a regional basis. However, adequate resources are not available to the Commission for such a programme and there is no likelihood of such resources becoming available in the foreseeable future.

#### PART I. RESOURCES REQUIRED

6. Any training programme requires resources for four major purposes:

Planning and general administration

Servicing of the meetings

Expenses of lecturers

Expenses of participants.

These four elements will be discussed in turn.

##### A. Planning and general administration

7. The United Nations does not have a centralized service for the organization of training programmes, seminars and symposia. Therefore, the Commission's Secretariat is responsible for the administration of all seminars or symposia sponsored by the Commission as well as for the planning of the substantive programme itself. Some organizations within the United Nations which sponsor a large number of training programmes have a separate organization for their administration. For example, the United Nations Industrial Development Organization has a Training Branch with nine professional officers and nineteen general service staff, a total number half again as large as the entire authorized personnel in the Commission's Secretariat. Therefore, unless the staff of the Commission's Secretariat were to be increased, any substantial expansion of the activities in training and assistance would be at the expense of other responsibilities of the Secretariat.

\* For consideration by the Commission see Report, chapter VII (part one, A, above).

\*\* 2 June 1981. Referred to in Report, para. 106 (part one, A, above).

<sup>1</sup> *Official Records of the General Assembly, Thirty-fifth Session, Supplement No. 17 (A/35/17)*, para. 162 (Yearbook . . . 1980, part one, II, A).

<sup>2</sup> The most recent General Assembly resolutions are 35/51 para. 9(c) (Yearbook . . . 1980, part one, II, D) and 34/142, para. 5(b) (Yearbook . . . 1980, part one, I, C).

<sup>3</sup> The First Symposium was held in 1975 on the occasion of the Commission's eighth session. The Second Symposium is being held in 1981 on the occasion of the Commission's fourteenth session.

<sup>4</sup> *Official Records of the General Assembly, Thirty-fifth Session, Supplement No. 17 (A/35/17)*, para. 155 (Yearbook . . . 1980, part one, II, A).

<sup>5</sup> *Ibid.*, para. 156.

### B. *Servicing of the meetings*

8. The servicing requirements for a symposium or seminar depend on the nature of the programme to be given. If a seminar is given in one language to a restricted group, it may require only that an adequate room be available. If, on the other hand, a seminar is to be conducted in several languages, simultaneous interpretation facilities must be available, as well as interpretation and translation of any necessary documents, and perhaps associated conference servicing staff.

9. If a symposium is organized at a United Nations location the meeting room and servicing requirements are furnished by the Conference Servicing Staff of the United Nations. Nevertheless, if the symposium is conducted in more than one language, the provision of interpretation and translation services entails extra cost to the United Nations which must be met from the regular budget of the organization.<sup>6</sup>

10. If the symposium is held at a different location, the conference servicing requirements would have to be furnished by local authorities. This would require that the Government or some organization with which the Commission might co-operate invite the Commission to hold its seminar at that location and agree to assume the local costs, including an adequate meeting room and interpretation, if necessary.

11. Depending on the nature of the programme to be given and the responsibilities to be undertaken by the inviting Government or organization, it might be necessary for a member of the Commission's Secretariat to travel to the intended location in order to co-ordinate the local arrangements.

### C. *Expenses of lecturers*

12. Representatives to the Commission and members of the Secretariat have given lectures in areas of their expertise at the two symposia held to date. Because the lecturers were already scheduled to be at the Commission session, there has been no expense to the United Nations for travel and subsistence.

13. If a seminar were held on a regional basis, it could be expected that some, and perhaps all, of the lecturers would have to be brought to the location of the seminar. In order to reduce the associated expenses, it would be desirable to reduce to a minimum the number of lecturers whose travel and subsistence would have to be assumed.

14. It could be expected as a result that the programme for a regional seminar might be somewhat different than it has been for the two symposia to date.

Because of the availability of lecturers with a wide range of expertise, it has seemed desirable for the symposia to cover the broad range of the Commission's activities. If the number of lecturers were to be reduced, it would probably be necessary to restrict the range of subject matter so that the same lecturer could more easily lead several sessions of the seminar. However, if lecturers other than members of the Secretariat were asked to lead several sessions of a seminar over a period of several days in length, it may be necessary to pay them an honorarium in addition to their travel and subsistence costs.

### D. *Expenses of participants*

15. The major direct cost for the two symposia sponsored by the Commission has been the reimbursement of travel and subsistence expenses of certain participants from developing countries. In addition, a number of participants have attended both symposia at their own expense.

16. Holding seminars on a regional basis would reduce to some extent the cost of sponsoring participants to attend the seminar. The amount by which those costs would be reduced would depend on a number of factors.

17. To the extent that the seminar would be held for the benefit of participants from the city in which it would take place, the travel and subsistence costs would be eliminated. To the extent that participants from other places in the region were sponsored by the Commission, the savings in costs would be essentially the difference in air fare between their home and the location of the seminar and their home and the location of the Commission, i.e. Vienna or New York. The amount of savings would depend on the location of their home and of the seminar.

18. Whether those savings would be equal to the extra expenses created by holding the seminar away from a United Nations location would depend on the location of the seminar, the number of participants to be brought from other locations at Commission expense, the number of lecturers to be brought to the seminar at Commission expense and the extra costs of administration. With such a large number of factors to be determined in regard to each seminar individually no generalization is possible.

## PART II. OTHER ADMINISTRATIVE CONCERNS

19. There are two other administrative concerns affecting all seminars and symposia to be sponsored by the Commission which the Commission may wish to consider.

<sup>6</sup> See paras. 20 to 22 below.

### A. Languages of symposium

20. The number of languages in which a symposium or seminar is held has implications both for the costs of the programme and for its content. The two symposia held to date have been in English and French with simultaneous interpretation. For the First Symposium in 1975, there were no financial implications because the interpretation was provided by staff assigned to the Commission session who were available at times the Commission did not meet. This was possible to arrange in 1975 because it was anticipated before the Commission session that the Commission would not hold two meetings a day throughout the entire three week period scheduled. However, from the viewpoint of the Symposium this was an unsatisfactory arrangement because it was not possible to schedule sessions of the Symposium until the Commission had decided on its meeting schedule. On several occasions it was necessary to reschedule sessions of the Symposium when the Commission changed its meeting schedule.

21. The Second Symposium has been furnished with translation of the lecture outlines and with its own team of interpreters at an estimated cost to the United Nations of \$19,000.<sup>7</sup> As a result, it has been possible to schedule various lecturers well in advance and this should have a beneficial effect on the substance of the programme.

22. If the Commission embarks on a regular programme of symposia or seminars, it may be desirable to hold them in a single language at a time, with the language used varying over time. This would be particularly desirable for regional seminars, but it may also be desirable for symposia held on the occasion of a Commission session. There would be both a reduction in costs to the United Nations and an increase in the ability of the participants to communicate among themselves. On the other hand, it may be more difficult to obtain sufficient lecturers in certain languages among the representatives to the Commission or the Secretariat.

### B. Financing of the programme

23. In order for the Commission to sponsor an effective programme of training and assistance, it must have an assured source of funds to cover the necessary direct expenses involved. These expenses include fellowships to participants from developing countries for travel and subsistence, travel and subsistence for lecturers sent to regional seminars and translation and interpretation if the seminars or symposia are to be held in more than one language at a time. Of these expenses, the United Nations has assumed only the translation and interpretation for the Second Symposium. However, since no provision for such expenses has been made in the regular budget of the Commission or its Secretariat, there is no assurance that these funds will be available in the future.

24. It cannot be expected that the expenses of the Commission's symposia or seminars can be met from the regular budget of the United Nations. Therefore, it would be strongly desirable that the programme of training and assistance in international trade law sponsored by the Commission either be endowed by a large grant, with interest or capital and interest to be expended over an extended period of time, or that individual States commit themselves to an annual contribution of a specific sum to the Commission's programme.

25. Such an assured source of financing would be of particular value in the planning of regional seminars where the variability of the expenses is greater than it is for a symposium organized on the occasion of a session of the Commission. However, experience has shown that even for a symposium to be held on the occasion of the Commission's session, it is difficult to plan efficiently when the amount of funds ultimately to be available and the date of their availability are uncertain.

26. Therefore, whatever decision the Commission might make in regard to symposia or regional seminars, it is vitally important to the success of the programme that the necessary funds be made available well in advance of its scheduled date.

<sup>7</sup> A/35/681.



## VIII. ALTERNATIVE METHODS FOR THE FINAL ADOPTION OF CONVENTIONS EMANATING FROM THE WORK OF THE COMMISSION

**Note by the Secretariat: alternative methods for the final adoption of conventions emanating from the work of the Commission (A/CN.9/204)\***

1. The Working Group on International Negotiable Instruments at its tenth session was of the view that at its eleventh session, which will be held in New York from 3 to 14 August 1981, it would probably be able to terminate the work on international negotiable instruments the Commission has conferred upon it.<sup>1</sup> The Working Group expects at that time to adopt two separate draft texts, the draft Convention on International Bills of Exchange and International Promissory Notes and the draft Uniform Rules Applicable to International Cheques, the two texts either to be set forth in a single draft convention or in two separate draft conventions.

2. The Working Group noted that it would accord with past practice for the Secretary-General to transmit the draft texts adopted by the Working Group upon their completion, together with a commentary, to Governments and interested international organizations for comment prior to their consideration by the Commission. However, after hearing a statement from the Secretary of the Commission on the desirability of simplifying if possible the procedures for the adoption of the texts as conventions, the Working Group suggested that, for the purpose of accelerating the work, the Commission might wish to consider whether it should request the Working Group to study and consider those comments and report to the Commission.<sup>2</sup>

3. In addition, the Working Group on International Contract Practices at its second session adopted draft Uniform Rules on Liquidated Damages and Penalty Clauses. The Working Group decided that the issue as to the final form in which the rules might be adopted should be left to the Commission.<sup>3</sup> The advantages and dis-

advantages of adopting the Draft Uniform Rules on Liquidated Damages and Penalty Clauses as a convention, as a model law or as recommendations are discussed in A/CN.9/203,\* paras. 114 to 122.

4. This note will discuss alternative procedures available for adopting a convention which emanates from the work of the Commission. This discussion is applicable to the texts which have been or will be adopted by both Working Groups. These texts differ from those previously adopted by the Commission for submission to a conference of plenipotentiaries in that the draft Uniform Rules on Liquidated Damages and Penalty Clauses are much shorter while the draft Convention on International Bills of Exchange and International Promissory Notes and the draft Uniform Rules Applicable to International Cheques are longer than were the earlier texts. This fact raises the question as to whether the past practice of the Commission in respect of its draft conventions is the most appropriate procedure to be used for these draft texts.<sup>4</sup>

5. If the Commission were to decide at its present session that the draft Uniform Rules on Liquidated Damages and Penalty Clauses would be adopted in the form of a convention, past practice would indicate that the draft rules, with a commentary prepared by the Secretariat, would be circulated to all States in the autumn of 1981 for comments. The comments would be received in the spring of 1982 and the Commission could consider the draft Uniform Rules and the comments thereon at its fifteenth session in 1982. The General Assembly might then be requested to convene a conference of plenipotentiaries of perhaps two weeks in duration to be held in 1984 to consider the draft text and adopt a convention.

6. If the Working Group on International Negotiable Instruments were to finish its work at its eleventh session

\* 12 May 1981. Incorporates A/CN.9/204/Corr.1 (English only) (21 May 1981). Referred to in Report, paras. 12, 39 (part one, A, above).

<sup>1</sup> Report of the Working Group on International Negotiable Instruments on the work of its tenth session, A/CN.9/196, paras. 208-209 (reproduced in this volume, part two, II, A).

<sup>2</sup> *Ibid.*, paras. 211-213.

<sup>3</sup> "Report of the Working Group on International Contract Practices on the work of its second session" (A/CN.9/197) (reproduced in this volume, part two, I, A).

\* Reproduced in this volume, part two, V, B.

<sup>4</sup> Some of the same issues were discussed in a Note by the Secretariat, "Alternative Methods for the Final Adoption of the Draft Convention on Prescription (Limitation) in the Field of International Sale of Goods" (A/CN.9/R.12) and by the Commission at its 123rd meeting (A/CN.9/SR.123).

in August as expected, and past practice were followed, the same pattern as above would take place except that the Commission would consider the texts at its sixteenth session in 1983 and the conference of plenipotentiaries would be held in 1985. If the two draft texts were to be given as thorough a review as was given the United Nations Convention on Contracts for the International Sale of Goods, a minimum of seven weeks should be scheduled both for the sixteenth session of the Commission in 1983 and for the conference of plenipotentiaries in 1985.

7. Although the Commission and a conference of plenipotentiaries gave a full review of the draft conventions originally prepared by Working Groups in the case of the Convention on the Limitation Period in the International Sale of Goods, the United Nations Convention on Carriage of Goods by Sea, 1978 and the United Nations Convention on Contracts for the International Sale of Goods, this three-level consideration and review was not followed in the case of the UNCITRAL Arbitration Rules or the UNCITRAL Conciliation Rules. In both cases the draft rules were considered in substance only by the Commission. The General Assembly subsequently recommended the use of the Rules as adopted by the Commission.

8. Therefore, in order to simplify the procedure for the adoption of the texts which the Working Groups have completed or soon will complete, it may be possible to reduce the scope of one of the two reviews of the text which would normally follow adoption by a Working Group.

9. In the case of the draft Uniform Rules on Liquidated Damages and Penalty Clauses, it is not suggested that a full review by the Commission be eliminated. However, in the case of the draft Convention on International Bills of Exchange and International Promissory Notes and the draft Uniform Rules Applicable to International Cheques, the Commission might decide, as suggested by the Working Group, that it should ask the Working Group to consider the observations of Governments and interested international organizations and make the changes in the texts deemed desirable as a result of those observations. The Commission might then adopt the draft texts without detailed discussion. It could be expected that the Working Group, which is thoroughly familiar with these relatively long and difficult texts, would be able to review the observations and make the necessary changes in less time than would be necessary in the Commission.

10. In this regard it may be noted that, on the basis of past practice, the draft texts will be circulated for comment to all States, including States non-members of the Commission. Furthermore, under the provisions of General Assembly resolution 31/99,\* para 10(c),

Governments of Member States of the United Nations that are not members of the Commission are entitled to attend the sessions of the Commission and its working groups as observers. The tenth session of the Working Group on International Negotiable Instruments was attended by observers from nine States members of the Commission, twelve States non-members of the Commission and five international organizations, in addition to the eight States members of the Working Group. Since the practice has been to allow observers to participate fully in the discussions in the Working Group, all interested States would have had an ample opportunity to participate in the preparation of the draft texts.

11. An alternative means of simplifying the procedure would be for the conventions to be adopted by the General Assembly on the recommendation of the Sixth Committee, rather than by a separate conference of plenipotentiaries. This would leave it for the Sixth Committee itself to make the detailed review of the draft Uniform Rules on Liquidated Damages and Penalty Clauses that would otherwise have been undertaken by a conference of plenipotentiaries. While in this case there would be no reduction in the number of reviews, it would nevertheless result in a reduction of some of the conference servicing costs of the United Nations in the following ways:

A separate conference of plenipotentiaries would devote a substantial portion of the two weeks to organizational matters which may be unnecessary in the Sixth Committee;

If the draft Uniform Rules were considered and adopted by the Sixth Committee, in-session conference servicing requirements would probably be met by the regular staff of the United Nations already allocated to the Sixth Committee. The extra costs for in-session conference servicing of a conference of plenipotentiaries would depend on the time and location of the conference. If the conference were held in Vienna, the presumable location of the conference since it is the location of the Commission's Secretariat, conference staff would mainly be brought from Geneva, as it was for the United Nations Conference on Contracts for the International Sale of Goods, with the attendant costs of travel and per diem. Pre-session and post-session costs of documentation would be the same whether the draft Uniform Rules were adopted by the Sixth Committee or by a separate conference of plenipotentiaries.

12. Costs for the States which participated in the adoption of the draft Uniform Rules as a convention would be approximately the same whether the Rules were adopted by the General Assembly or by a conference of plenipotentiaries since it could be expected that most States would find it necessary to send specialists in private law to attend those sessions of the Sixth Committee devoted to a consideration of the Uniform Rules.

\* Yearbook . . . 1977, part one, I, C.

13. It cannot be anticipated whether the Sixth Committee would be willing to undertake a detailed examination of the draft Uniform Rules on Liquidated Damages and Penalty Clauses in 1984, the year the rules are expected to be ready for consideration and adoption as a convention. However, if the Commission were of the view that consideration by the Sixth Committee would be desirable, it would be appropriate for the Commission to make such a recommendation.

14. However, it would not be feasible for the Sixth Committee to conduct an article by article examination of the draft Convention on International Bills of Ex-

change and International Promissory Notes and the draft Uniform Rules Applicable to International Cheques.

15. In considering the issues involved in this note, the Commission may wish to bear in mind resolution 35/10C in which the General Assembly

"1. *Invites* Member States and United Nations organs, when considering the convening of special conferences, to ensure that the objectives of the proposed conference are such that they have not been achieved and cannot be pursued within a reasonable time-frame through the established intergovernmental machinery of the United Nations and the specialized agencies;"

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#### IV. CHECK LIST OF UNCITRAL DOCUMENTS

##### List of documents before the Commission at its fourteenth session

<i>Title or description</i>	<i>Document symbol</i>	<i>Location in present volume</i>
<b>A. GENERAL SERIES</b>		
Provisional agenda, annotations thereto and tentative schedule of meetings; note by the Secretary-General	A/CN.9/195	Not reproduced
International Payments: report of the Working Group on International Negotiable Instruments on the work of its tenth session (Vienna, 5-16 January 1981)	A/CN.9/196	Part two, II, A
Report of the Working Group on International Contract Practices on the work of its second session (New York, 13-17 April 1981)	A/CN.9/197 and Corr.1 (Russian only)	Part two, I, A
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